

Message from the Special Inspector General for Iraq Reconstruction

I am pleased to submit to the Congress this combined Quarterly and Semiannual Report of the Office of the Special Inspector General for Iraq Reconstruction (SIGIR), which complies with the reporting requirements of Public Law 108-106, as amended, and the Inspector General Act of 1978 (P.L. 95-452). This Report documents the important progress SIGIR has made since the April 30, 2005 Quarterly Report, and it updates the status of coalition reconstruction efforts in Iraq, which are now primarily funded by the Iraq Relief and Reconstruction Fund (IRRF). Of note, contractual obligations of the IRRF grew during this reporting period from 66% to 75%, and expenditures increased from 23% to 35%.

The current phase of the Iraq reconstruction program is now peaking. Over 1,000 projects are finished, and another 1,000 are underway. Thus, effective oversight is essential to ensure the continued success of our reconstruction program in Iraq. I am committed to providing constructive, “real time” advice that helps the Chief of Mission and his managers of Iraq reconstruction to succeed. And I am doing my level best to detect and deter fraud, waste, and abuse in Iraq.

During this past quarter, I conducted my eighth trip to Iraq—a very successful visit—and I will return there again in August. I currently spend about a third of my time in Baghdad, supervising the continuing execution of our substantial oversight mission. The SIGIR now has in Iraq 18 auditors (managing 11 audits), 9 investigators (managing 56 cases), and 5 evaluators (managing a series of project assessments). We are the largest oversight entity in Iraq. We are there because we have an enormous mission—serving as the taxpayers’ watchdog over approximately \$21 billion in U.S. investment in Iraq’s reconstruction. I am grateful that the State Department recently agreed to permit the SIGIR to station up to 45 personnel in Baghdad: this staff level is essential to our success.

In Iraq, SIGIR auditors continue to identify critical issues that hinder the success of the reconstruction program and, pursuant to my direction, they are rapidly communicating their recommendations to reconstruction managers. Our aggressive approach to auditing, which clearly has a consultative component, seeks to provide the benefits of oversight in time to make a money-saving difference. The SIGIR hopes to correct inefficiencies as they are found, rather than wait for a final report. This approach, necessary because of the limited duration of our mission, steps beyond traditional inspector general practices to an activist posture that more effectively promotes efficiency and economy.

During this past quarter, SIGIR has progressed in several important areas:

- developing and deploying teams of auditors and engineers to rapidly assess completed reconstruction projects in order to determine whether the U.S.

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government received proper value for its investment (The SIGIR's first four assessments are summarized in this Report.)

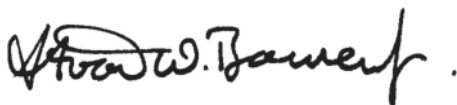
- expanding our investigations capacity by recruiting and deploying highly experienced investigators who now work closely with the Department of Justice to pursue prosecutions
- forming a task force—designated SPITFIRE (Special Investigative Task Force for Iraq Reconstruction)—that applies the considerable experience of the member organizations to recover improperly diverted Iraq reconstruction assets and to detect and investigate fraud and other crimes
- continuing to develop SIRIS (the SIGIR Iraq Reconstruction Information System), which will provide a single consolidated database of financial, project, and contract information on Iraq reconstruction
- appearing for the first time before the Congress and providing testimony on the current status of Iraq reconstruction

We continue to take the initiative on two other important issues: the lack of reliable estimates of the cost to complete projects and the sustainability of completed projects. We have already completed a final audit on cost to complete, included in this Report, which examines whether IRRF accounting and reporting systems are adequate to determine the cost to complete for current or planned projects. We have also announced a series of new audits that will look at the issue of sustainability.

As this Report goes to press, I am pleased to learn that the Senate has approved an amendment to the FY 2006 Foreign Operations appropriations bill that would enable the SIGIR to continue its important oversight mission. Current law establishes our “sunset” at 10 months after 80% of the IRRF has been contractually obligated. Under this measure, the SIGIR could terminate by next spring, well before much of the IRRF is expended. The new amendment, if passed, will extend the SIGIR's mission until 80% of the IRRF has been expended.

The SIGIR continues to carry out the mission that the Congress assigned to it, with vigor, speed, and efficiency; we will continue to do so as long as the Congress and the Administration see fit.

Submitted on July 30, 2005

A handwritten signature in black ink, reading "Stuart W. Bowen, Jr." with a stylized flourish at the end.

Stuart W. Bowen, Jr.
Special Inspector General for Iraq Reconstruction

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Section 1

Executive Summary

Executive Summary

Executive Summary

During this reporting period, the Special Inspector General for Iraq Reconstruction (SIGIR) has conducted audits and investigations to prevent fraud, waste, and abuse in the programs and operations funded by the Iraq Relief and Reconstruction Fund¹ (IRRF). The SIGIR continued to aggressively promote economy, efficiency, and effectiveness in the administration of programs funded by the IRRF.

Since the April 2005 Quarterly Report, the SIGIR has increased its capability to provide independent and objective leadership to coordinate the diverse activities of the multiple agencies and organizations involved in Iraq reconstruction.

The Status of Iraq Reconstruction

As the reconstruction effort in Iraq matures and shifts focus from planning and design to implementation and handover, U.S. agencies must ensure that their efforts leave the Iraqis with a firm foundation on which to build. During this reporting period, the SIGIR continued to conduct discussions and interviews with key members of Iraq reconstruction management teams in Baghdad and Washington, D.C. Based on first-hand knowledge of the current situation in Iraq, existing SIGIR initiatives, and continuing oversight work, the SIGIR is actively pursuing two emerging issues:

- *Cost to complete:* Can the U.S. government agencies managing Iraq reconstruction projects produce reliable estimates of the costs of completing those projects (and thus avoid over-obligating funds)?
- *Sustainability:* Can reconstruction projects funded by the U.S. government be sustained after handover to the Iraqis?

A failure on either of these points puts at risk the important legacy of success that the U.S. intends to leave. As of July 5, 2005, approximately 75% of the \$18.4 billion IRRF had been obligated, and 35% had been disbursed.

During this quarter, the SIGIR increased efforts to address a persistent set of challenges facing the agencies and organizations involved in Iraq reconstruction:

- *Strategy and Interagency Coordination:* At least a dozen offices representing six U.S. agencies directly spend money from the IRRF. There is minimal, if any, integration among the various systems that these offices use to manage information on contracting, finance, and projects.

- *Program Management:* Inadequate processes, systems, documentation, training, and internal controls are regularly cited in oversight reports on Iraq reconstruction. To make informed, effective decisions, management requires more reliable data.
- *Acquisition and Contract Management:* The SIGIR is concerned that insufficient internal controls have created conditions for mismanagement, inefficiencies, and ineffectiveness in acquisition and contract management.
- *Human Resources:* The SIGIR has observed that Iraq reconstruction efforts continue to be hampered by high turnover of key personnel and vacancies in critical positions.
- *Security:* Providing security continues to exact a heavy cost on Iraq reconstruction, slowing reconstruction efforts and reducing the potential impact of reconstruction.

The threat to life and property from continuing insurgent attacks remains a major impediment to the reconstruction and rehabilitation of Iraq. As of June 30, 2005, 330 contractors had been killed in Iraq. During this reporting period, the total number of Defense Base Act insurance claims grew by more than 30%, and death claims rose by 20%. The rising number of claims underscores both the danger inherent in reconstruction activities and the continuing costs arising from the current environment.

SIGIR Oversight Activities

The SIGIR completed five audits this quarter, and nine audits are ongoing. These are brief overviews of some of the major audits conducted during this reporting period:

Reconciliation of Reporting Differences of the Source of Funds Used on Contracts after June 28, 2004

(Report No. 05-009, issued July 8, 2005)

The SIGIR examined contracts to determine if they improperly obligated DFI funds after June 28, 2004. The SIGIR concluded that the 48 contracts reviewed disclosed no instances of incorrect obligations of DFI funds. In 39 contracts, the obligations of DFI occurred before June 28, 2004. Obligations for the remaining nine contracts did not cite DFI funds but rather U.S. funds appropriated by the Congress. The obligation documents for the six contracts identified as the Multi-National Corps-Iraq cited Commanders' Emergency Response Program funds, and the other three contracts cited the IRRF as the source of the funding.

The SIGIR also concluded that the Joint Contracting Command-Iraq (JCC-I) current contract data files were not accurate and not adequately supported. Our review showed that 48 of the 69 contracts contained data entry errors in documenting the date of the contract award or the source of the funding.

Interim Briefing to the Project and Contracting Office and the Joint Contracting Command-Iraq on Award Fee Process
(Report No. 05-010, issued July 26, 2005)

The SIGIR conducted an audit of the PCO and JCC-I award fee process on design-build and program management and support contracts. The SIGIR reviewed 18 cost-plus-award fee contracts, valued at about \$6.9 billion. Although the PCO and the Joint Contracting Command-Iraq (JCC-I) had established an award fee evaluation board, as well as policies and procedures, there were a number of inconsistencies in the application of the policies and procedures.

This report made five recommendations.

Cost-to-Complete Estimates and Financial Reporting for the Management of the Iraq Relief and Reconstruction Fund
(Report No. 05-011, issued July 26, 2005)

The SIGIR conducted this audit on cost-to-complete data. The Section 2207 Report on Iraq Relief and Reconstruction (*Section 2207 Report*) for April 2005, compiled by the IRMO, did not meet the congressionally mandated requirement to include estimates, on a project-by-project basis, of the costs required to complete each project. As a result, without current and accurate cost-to-complete data, the funds available for the completion of the IRRF program cannot be determined and the availability of funds for the initiation of new projects cannot be projected. Inaccurate cost-to-complete estimates could result in needed projects being delayed or not built.

The accuracy of the \$7.9 billion of Department of Defense obligations reported on the *Secretary of the Army Report* issued March 27, 2005, and the *Section 2207 Report* for April 2005 could not be verified. The transactional data that was provided to support obligations reported in the *Secretary of the Army Report* for our review was not reconcilable and consequently did not meet objectives. The SIGIR subsequently learned in conversations with PCO finance that the *Secretary of the Army Report* (which is incorporated into the *Section 2207 Report*, consolidating Department of Defense financial reporting of IRRF funds) does not require certification for accuracy by PCO management.

This report made five recommendations.

Policies and Procedures Used for Iraq Relief and Reconstruction Fund Project Management – Construction Quality Assurance
(Report No. 05-012, issued July 22, 2005)

The Project and Contracting Office and the U.S. Army Corps of Engineers, the two major organizations involved in Iraq Relief and Reconstruction Fund (IRRF) projects, have established written policies and procedures for

establishing and managing construction quality management programs for projects managed and funded by the IRRF.

The SIGIR plans to conduct additional reviews to determine the effectiveness of these policies and procedures as applied, and the adequacy of their coordination.

This report made no recommendations.

Since April 2005, the SIGIR caseload for *investigations* has increased significantly. Ten cases were closed this quarter, and the number of open cases rose to 56. In partnership with other law enforcement agencies, the SIGIR also created the Special Investigative Task Force for Iraq Reconstruction (SPITFIRE) to enhance its ability to detect fraud, trace international money transactions, and monitor travel. The SPITFIRE will pursue potential criminal activity in Iraq reconstruction funding with its partners: the Department of Homeland Security and the U.S. Department of State Office of Inspector General.

To ensure that U.S. taxpayers and Iraqi citizens are getting value for the dollars spent on U.S.-funded projects across Iraq, the SIGIR created a multi-faceted *project assessment program*. Unlike SIGIR auditors and investigators—who generally focus on programmatic issues and criminal acts, respectively—this new unit focuses on the actual work completed at specific projects in Iraq. During this reporting period, the SIGIR completed project assessments of the in-process work being performed on four projects in the water sector.

The SIGIR continues to develop the *SIRIS (SIGIR Iraq Reconstruction Information System)*—a much-needed tool for oversight analysis in Iraq. When complete, the SIRIS will provide a complete, standardized view of financial, contract and project information across all agencies and facilitate oversight of the IRRF. The SIGIR has begun a major data-gathering effort to populate this system.

Significant progress has been made in the SIGIR *Lessons Learned initiative*, compiling more than 3,600 references that capture the challenges, concerns, and risk factors that have confronted U.S. government organizations engaged in relief and reconstruction operations in Iraq. The SIGIR will host a series of Lessons Learned Forums in Washington, D.C., in which panels of experts and policymakers will review and evaluate the data gathered by the SIGIR, evaluate it, and make recommendations. The first Lessons Learned Forum will be held in September 2005 and will address Human Resources. The SIGIR is also planning forums focusing on Program and Financial Management, and Contracting and Acquisitions.

As a strong advocate for *Iraq's anti-corruption organizations*, the SIGIR continued to assist the planning, development, and training of the Iraqi Inspector General (IG) system and to develop a useful dialogue with the

Commission on Public Integrity (CPI) on investigations, training, and other areas of mutual interest. The Iraqi IG system, the CPI, and the Board of Supreme Audit lead Iraq's efforts to prevent corruption, fraud, waste, and abuse.

The SIGIR Reports to the Congress are available on the *SIGIR Website* (www.sigir.mil) in English and Arabic. (This report will be translated and posted within 60 days of release.) During this reporting period, the SIGIR expanded the content provided in Arabic, including a section of the website now completely navigable in Arabic and translations of most recent SIGIR audits.

The Objectives of This Report

This July 30, 2005 Report fulfills the requirements of the Inspector General Act of 1978 for semiannual reporting and of Public Law 108-106, as amended, for quarterly reporting to the Congress. This Report includes:

- a presentation of current, final, and planned audits
- an overview of investigative activity
- a narrative of reconstruction activities
- updates on the SIGIR's major initiatives
- a detailed summary of Iraq funding data collected and analyzed by the SIGIR
- key information on major Iraq reconstruction contracts

An Overview of This Report

This Report is organized in these sections and subsections:

Section 1: Executive Summary

Section 2: Iraq Reconstruction Update

- Cost to Complete and Sustainability
- Continuing Challenges to Reconstruction
- Status of Reconstruction Funding
- Measuring Outcomes

Section 3: SIGIR Oversight

- SIGIR Mission and Duties
- SIGIR Audits
- SIGIR Investigations
- SIGIR Project Inspection Program
- SIGIR Hotline
- Other SIGIR Activities and Initiatives

Section 4: Other Agency Oversight

Appendices



SIGIR TEAM TOURS WATER PLANT – An assessment team from the SIGIR inspects new construction at a central Iraq water treatment plant. SIGIR's engineer, auditor, and special agent determine the progress made in upgrading the facility with Iraq Relief and Reconstruction Funds and whether the upgrades meet contractual requirements.

Section 2

This section presents the SIGIR's overview of the current state of Iraq reconstruction.

Section 2 covers these topics:

- Overview
- Cost to Complete and Sustainability
- Continuing Challenges to Reconstruction
- Status of Reconstruction Funding
- Measuring Outcomes

Overview

The goal of U.S. reconstruction efforts in Iraq is to promote a stable and prosperous Iraqi democracy. The Iraq Relief and Reconstruction Fund (IRRF) and other U.S. and international aid are a first step in that process, but they will certainly not meet all of Iraq's development needs. In October 2003, a joint UN-World Bank assessment estimated that post-war Iraq required almost \$60 billion in investment to restore the country. The coalition investment will accomplish only part of that goal. Ultimately, a stable, prosperous, and democratic Iraqi government must implement its own comprehensive, long-term reconstruction program before the nation can achieve its tremendous potential. Nevertheless, the IRRF is a substantial down-payment toward that goal.

As the reconstruction effort matures and shifts focus from planning and design to implementation and handover, U.S. agencies must ensure that their efforts leave the Iraqis with a firm foundation on which to build. Moreover, they must determine whether sufficient funds exist to complete the projects begun in Iraq and whether these projects include a sustainability plan that will provide the Iraqis with the tools and knowledge necessary to operate and maintain their new infrastructure. A failure on either of these points risks leaving little to show for billions in U.S. infrastructure investment. As of July 6, 2005, approximately 75% of the \$18.4 billion IRRF had been obligated, and 35% had been disbursed.

Cost to Complete and Sustainability

During this reporting period, the Special Inspector General for Iraq Reconstruction (SIGIR) has continued to conduct discussions and interviews with key members of Iraq reconstruction management teams in Baghdad and Washington, D.C. Based on first-hand knowledge of the current situation in Iraq, ongoing SIGIR initiatives, and continuing oversight work, the SIGIR is pursuing two key issues, among other concerns, during management interviews:

- Can the U.S. government agencies managing Iraq reconstruction projects produce reliable estimates of the costs of completing those projects (and thus avoid over-obligating funds)?
- Can U.S. government-funded reconstruction projects be sustained by the Iraqis?

The first of these issues was raised in the SIGIR April 2005 Report to Congress; both issues received prominent mention in the July 2005 *Section 2207 Report* on Iraq reconstruction, released by the Department of State (DoS). Also, they are regularly addressed at internal reconstruction management briefings attended by SIGIR representatives.

The SIGIR's interest in securing accurate cost-to-complete estimates has produced action. Since as early as February 2005, the SIGIR has been asking for cost-to-complete data but has yet to receive any reliable data responsive to these requests. Officials at the Project and Contracting Office (PCO) have cited a number of constraints hindering development of cost-to-complete estimates, including:

- difficulty integrating data among financial and project management information systems
- incomplete program management data
- rapidly rising security costs

To press the cost-to-complete issue, the SIGIR audited the information systems of the Iraq Reconstruction Management Office (IRMO) and the PCO, addressing cost-to-complete estimates from reconstruction agencies. This audit concluded that the systems failed to produce the needed cost-to-complete data; therefore, the mandated reporting requirement was not met. Also, the audit concluded that without current and accurate cost-to-complete data, the funds available for the completion of the IRRF program cannot be determined and the availability of funds for the initiation of new projects cannot be projected².

During this quarter, the Department of State (DoS) announced that it has implemented a comprehensive cost management plan to ensure that projects can be completed with available funds. The IRMO has also recently reported that the IRMO, PCO, and U.S. Agency for International Development (USAID) are preparing a memorandum of understanding on cost-to-complete reporting. An ongoing SIGIR audit will address cost-to-complete estimates in more detail.

The SIGIR also has announced a new series of audits to address sustainability issues. These audits will ask whether U.S. government organizations have developed and approved plans to fund and support the transition and sustainment of completed projects and whether these plans are being implemented at the sector and project level.

The growing recognition of the importance of sustainability is reflected in management's actions as well. For example, the DoS reports that it has initiated a program to review turnover procedures for contracts and is beginning to plan for the handover of completed IRRF projects.

Defining the Terms

Although reconstruction management has examined the issues of cost to complete and sustainability, the SIGIR has observed that the terms are frequently used inconsistently. Without a common frame of reference, each implementing agency has addressed these issues in its own way. As a result, it may be difficult to compare reports prepared by different agencies.

To offer reconstruction agencies a common vocabulary, the SIGIR proposes the use of internationally accepted definitions for these two terms. A SIGIR team consulted multiple sources to identify the most appropriate definitions for the Iraq reconstruction challenge. To define cost to complete, the SIGIR referenced the Project Management Institute's standards document, *A Guide to the Program Management Body of Knowledge* (PMBOK), and the American Production and Inventory Control Society (APICS) dictionary. To define sustainability, the SIGIR relied on colleagues in other federal agencies, including the USAID and the World Bank.

Cost to Complete

The cost to complete a project may be defined as the total estimated cost of the project less the actual cost of work performed to date:

- The estimated cost of the project is the actual direct cost, plus indirect costs or allocable costs to the contract, plus the estimate of costs (direct and indirect) for authorized work remaining.
- The actual cost of work performed to date is the cost (direct and indirect) to date of completed work packages and the completed portion of work packages begun and not yet completed.

Sustainability

Sustainability may be defined as the ability of a program to deliver its intended benefits for an extended period of time after major financial, managerial, and technical assistance from an external donor is terminated.

Continuing Challenges to Reconstruction

Since 2003, the U.S. reconstruction effort has faced a set of persistent challenges inherited by a succession of U.S. agencies. Although each of these issues affects reconstruction efforts, it is likely that many cannot be solved within the timeframe of the Iraq reconstruction effort. The SIGIR has identified several of these issues as highly relevant to the questions of cost to complete or sustainability and, thus, to the successful handover of U.S. projects:

- Strategy and Interagency Coordination
- Program Management
- Acquisition and Contract Management
- Human Resources
- Security

Some of these issues have received extensive attention from oversight agencies; others are ripe for additional research. As part of its on-going effort to coordinate oversight of reconstruction, the SIGIR has cataloged the 57 audits published by the SIGIR and 5 other agencies auditing Iraq reconstruction. The SIGIR has grouped these audits into general categories to give a rough overview of their scope. Figure 2-1 details the audits in each category and also segments the audits from the period before the June 28, 2004 transfer of governance authority from those that cover later data.

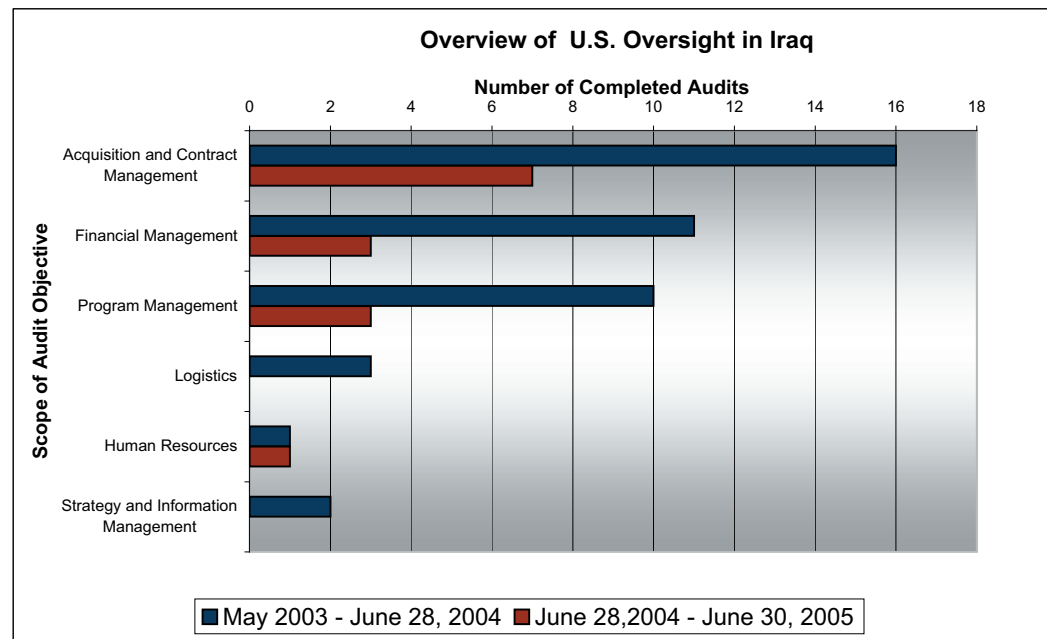


Figure 2-1

For the SIGIR's audit summary and a complete list of the Iraq reconstruction reports, see Appendix J.

As part of an ambitious initiative, the SIGIR will address many of these issues in a series of upcoming forums that seek to derive key lessons learned from the Iraq reconstruction experience. These panels of experts from the U.S. government, industry, and academia will evaluate the findings compiled by the SIGIR and will provide recommendations in separate reports on how to better meet the challenges posed by the reconstruction of Iraq. At the end of the program, the SIGIR will publish a history of the Iraq reconstruction program.

Strategy and Interagency Coordination

At least a dozen offices representing six U.S. agencies directly spend money from the IRRF. There is minimal, if any, integration among the various systems that offices use to manage information on contracting, finance, and projects. This leaves the IRRF subject to uncoordinated management by “stove-piped” systems and can result in waste and duplication of efforts.

For an overview of IRRF funding authority, see Figure 2-2. For more detail about how U.S. and international funds are being spent in Iraq, see Appendices C, D, E, and F.

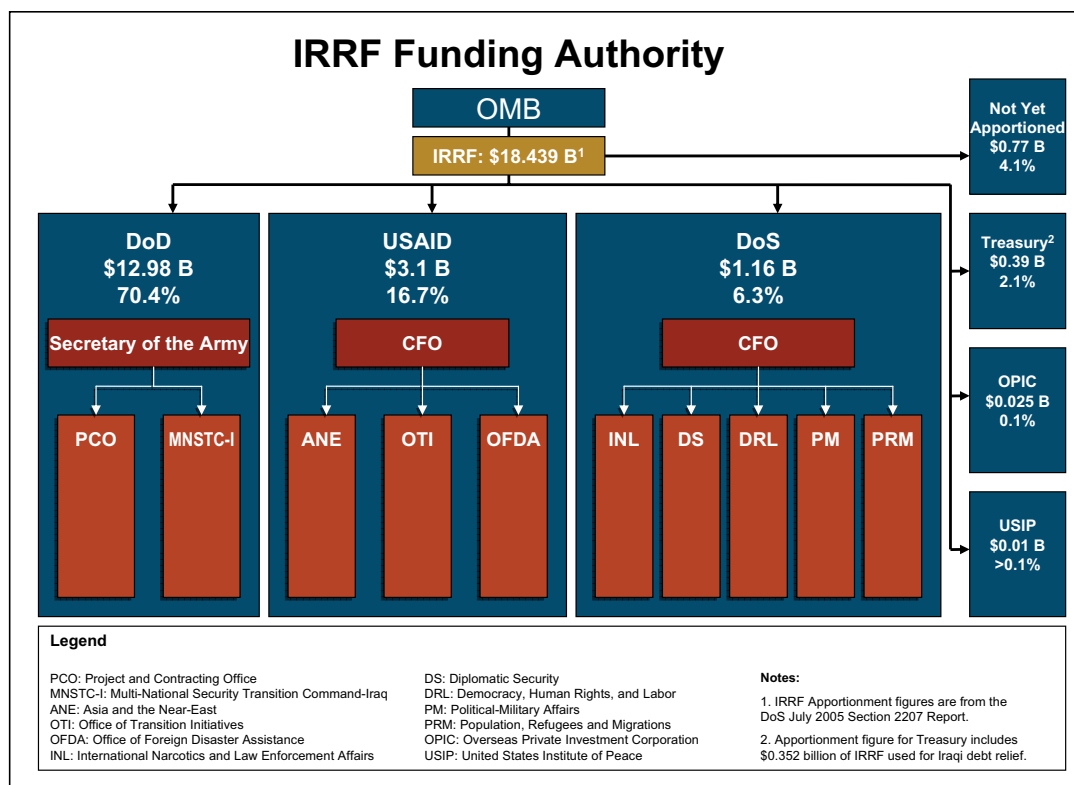


Figure 2-2

Impact of Funding Changes

As it has in each of the previous *Section 2207 Reports*, the DoS again notified the Congress in July 2005 that it will be reallocating IRRF dollars to adapt to changing mission requirements. Although flexibility in dealing with an unstable environment is essential, the SIGIR is interested in the cost impact of changing direction in the middle of a large undertaking. Money spent on planning, contracting, and other preparatory activities related to cancelled or changed projects usually cannot be recovered. Before pursuing changes, planners must weigh the time required to design new programs and award new contracts or task orders against other policy goals—including getting funds flowing to the Iraqi people.

The DoS stated in its July *Section 2207 Report* that “implementation of last quarter’s programmatic changes has been slow,” and it appears that some of the initiatives created by these changes may not become fully operational for several more months. The SIGIR questions whether these funding changes are reaching a point of diminishing returns and whether projects created in future reallocations will ramp up too late and save too little money to be worthwhile. Table 2-1 outlines major IRRF funding changes.

Major IRRF Funding Changes, as of July 5, 2005 (in millions)		
Date	Amount	IRRF Sectors Affected
September 2004	\$3,460	Water and electricity sectors reduced. Security, justice, education, private development sectors increased. Oil sector reallocated.
December 2004	457	Electrical sector reallocated. Battle damage remediation for Fallujah, Sadr City, Najaf, and Samarra.
March 2005	832	Job creation, operations and maintenance (O&M) for water and power, electricity and oil, cost growth by contractors.
July 2005	255	Reallocate funds to create Provincial Reconstruction Development Committees, train security forces, and support elections.
Total	\$5,004	
Note: Data not formally reviewed or audited.		

Table 2-1

Seeking cost savings by reallocating money from active projects can result in inefficiencies. For instance, a preliminary SIGIR project assessment of a water project—a sector that has experienced approximately \$3 billion in reallocations—found that, because of a reduction of scope, the project will not increase the quantity of water provided by the site or elevate the quality of the water to potable standards. Further, the assessment found that the design was not adequate to complete a fully functional water treatment facility³.

Audits by other agencies have reached similar conclusions. A recent USAID audit of electricity generation projects—another sector that has seen significant reallocations—showed that a project that was cancelled to save costs still incurred \$69.4 million in costs although little was actually achieved⁴.

Program Management

Inadequate processes, systems, documentation, training, and internal controls are regularly cited in oversight reports on Iraq reconstruction. At the heart of many of these findings is a concern that management does not have adequate information systems to support decision-making about the projects, contracts, and financing of Iraq reconstruction. If these systems do not provide reliable data, management cannot make informed, effective decisions.

The SIGIR will review these and other program management issues in greater depth in an upcoming Lessons Learned Forum. Meanwhile, the SIGIR is continuing an ongoing audit to review the information systems used by reconstruction agencies to track data on projects.

Information Systems and Data Discipline

Public Law 108-106 (P.L. 108-106) mandated deployment of management information systems capable of satisfying congressional reporting expectations. Through a series of audits, the SIGIR continues to investigate whether these systems can produce reliable data for management. The SIGIR has identified several potential problems:

- inaccurate reporting (data entry errors and inadequate controls)
- multiple information systems in Iraq that cannot interoperate
- significant time lags before changes are reflected in systems of record
- lack of interagency coordination on data management
- inconsistent data definitions

Figure 2-3 details the systems used by each agency for contract, project, and financial management.

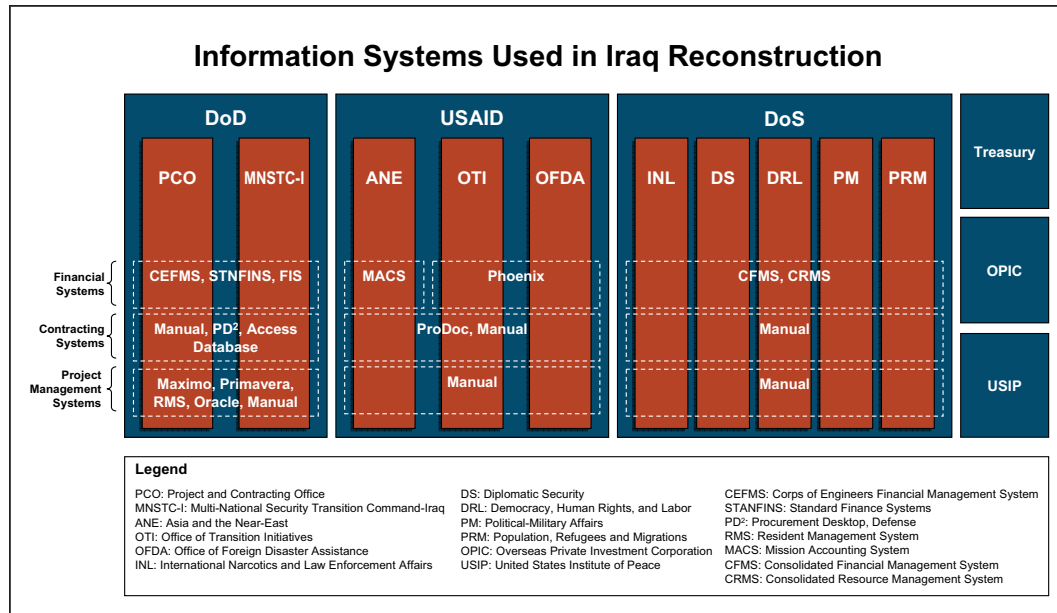


Figure 2-3

In a recently completed audit of cost-to-complete estimates, the SIGIR cites systems and data problems as a major contributor to the lack of meaningful and complete information. During the audit, program management officials cited incomplete program management data as an impediment to developing cost-to-complete estimates. PCO officials noted that as of March 31, 2005, of the largest 151 construction projects, only 67 (approximately \$2.4 billion) had established realistic baseline schedules and targeted costs to manage and forecast costs. The remaining 84 projects, totaling approximately \$2 billion, were planned but had not established realistic baseline schedules and targeted costs⁵.

In response to this audit, management noted ongoing efforts to integrate financial and project management systems. Management also noted that this effort has been difficult and that this difficulty contributed to the inability to provide accurate cost-to-complete data.

The systems used to track reconstruction projects remain highly dependent on manual data entry. The SIGIR is concerned that systems maintain adequate audit trails of manual entries. The SIGIR's preliminary project assessments have also identified projects that have been reduced in scale, but whose progress reported in data systems was never updated because the progress numbers are entered manually rather than being tied to specific project milestones in the system⁶.

Deploying and configuring management information systems is a complex, multi-year effort in peacetime; successfully assembling such a system in a war zone is an extremely ambitious undertaking. Because of the temporary nature of the reconstruction enterprise, it is essential that reconstruction agencies

focus on building a management process that is simple and can produce sufficiently reliable data to ensure the completion and handover of projects.

Acquisition and Contract Management

The SIGIR is concerned that insufficient internal controls have created conditions for mismanagement, inefficiencies, and ineffectiveness in acquisition and contract management. For instance, during this reporting period, the SIGIR conducted a review of the management of contract award fees. These fees are intended to reward above-average performance, but in instances reviewed by the SIGIR, award fee evaluation criteria were not clearly identified and performance indicators or metrics were not defined. Further, the Award Fee Plan did not provide incentives for the contractor to strive for quality efforts towards a superior performance⁷. The SIGIR's reviews of construction projects have revealed other instances of inadequate controls and procedures. For example, preliminary assessments of water projects have found that government project engineers—who can verify whether work has been completed properly—were not involved in approving invoices⁸.

The SIGIR has also found material management-control weaknesses in the administration of IRRF contracts. During an audit of contract administration that was summarized in the SIGIR April 2005 Report, the SIGIR identified significant deficiencies in processes and controls, including a number of contract files that could not be located. As a result, there was no assurance that contract file data:

- was available, complete, consistent, and reliable
- or*
- could be used effectively to monitor and report the status of IRRF projects

The SIGIR found that because of these weaknesses, there was no assurance that fraud, waste, and abuse did not occur⁹. Management reports taking corrective action to address these issues, and the SIGIR looks forward to reviewing the results.

Human Resources

The SIGIR has observed that Iraq reconstruction efforts continue to be hampered by high turnover of key personnel and extended vacancies in critical positions. Institutional knowledge is not consistently passed on by departing personnel. New staff often require extensive, resource-intensive “on-boarding” to become fully effective in their posts. These factors compound the problem:

- Many agencies have short staff rotations.
- Often, personnel filling assignments do not have continuity with predecessors or successors. Hand-off processes are not always effective; in some cases, there are no hand-off processes.

This inefficient cycle imposes a significant burden on the remaining staff to maintain continuity. Internal management reviews have also noted this issue within IRMO, suggesting that it threatens continuity, project execution, and critical relationships with Iraqi Ministry personnel.

To address this important issue, the SIGIR will focus the first Lessons Learned Forum on human resources issues. The forum will be held in Washington, D.C., in September 2005.

Security

Providing security continues to exact a heavy cost on Iraq reconstruction, slowing reconstruction efforts and reducing the potential impact of reconstruction. Continuing threats require that funds be re-allocated from reconstruction projects to security, thus reducing the potential number of projects that can be completed. The July DoS *Section 2207 Report* estimates that security costs amount to 16-22% of total costs for construction projects in Iraq. The Report also lists water, health care, and roads/bridges/construction projects that were canceled because funds were shifted to security.

In addition to reducing funds available for construction projects, rising security costs make it more challenging to estimate the costs to complete projects. PCO management has advised that, as of March 31, 2005, the estimated cost for project security had risen from the original program baseline of \$1.2 billion to more than \$2 billion¹⁰. The SIGIR believes that actual costs (e.g., delays caused by security problems, higher force levels than expected) are much higher.

For more information on security and insurance issues, see Section 3.

Status of Reconstruction Funding

Public Law 108-106, as amended, requires the SIGIR to report on the oversight and accounting of the obligation and expenditure of funds used for Iraq reconstruction. The three main sources of funds used for this are U.S. appropriated funds, donor funds, and Iraqi funds:

- *U.S. appropriated funds:* \$30.00 billion
- *Iraqi funds:* \$32.75 billion, primarily for the operation of the Iraqi government
- *Donor funds:* \$17.34 billion

As of June 30, 2005, approximately \$32.62 billion of U.S. and international donor funds had been pledged for Iraq reconstruction (excluding pledged bilateral support and humanitarian aid.) An estimated \$32.75 billion of Iraqi funds is available for the operation of the Iraqi government. Figure 2-4 presents summary information about sources of funding for Iraq reconstruction, as of June 30, 2005.

U.S. Appropriated Funds (\$30.00 Billion)	Iraqi Funds (\$32.75 Billion)	Donor Funds (\$17.34 Billion)
Public Law 108-11 (April 2003) - IRRF (\$2.475) - NRRRF (\$.802) - CPA OPS (\$.573) - New Iraqi Army (\$.051) Other Non-IRRF - USAID Programs (\$.412) ^a - DoS (\$.066)	Vested Funds - From Frozen Funds (\$1.724)	Donor (\$13.871) - Pledged bilateral support of loans and grants for Iraq reconstruction
Public Law 108-106 (Nov 2003) - IRRF (\$18.439) - CPA Operations (\$.769) - SIGIR (\$.075) - IRMO (\$.129) ^b - CERP (\$.140) ^c	Seized Funds - Confiscated Cash and Property (\$.927)	Firm Commitments, and Deposits, or Donations - Bilateral Assistance (\$1.120) - Emergency Post Conflict Assistance for IMF (\$.436) - Commitments to IRFFI (\$1.065)
Public Law 108-287 (Aug 2004) - CERP (\$.368) ^d	DFI (\$30.100)^e (Development Fund for Iraq) - Oil Proceeds ^f - Oil For Food (OFF) - Repatriated Funds	Humanitarian Aid (\$.849)
Public Law 109-13 (May 2005) - Iraq Security Forces Fund (\$5.700)		

^a USAID funding from P.L. 108-11 in addition to \$1,818 million received from FY 2003 IRRF
^b IRMO includes \$23.7 million for reporting requirements.
^c as of June 30, 2005
^d as of June 30, 2005
^e as of January 5, 2005; estimate includes non-DFI non-oil revenue of \$310 million.
^f CY 05 Iraqi oil revenue estimated at \$10.35 billion.
 NOTE: Numbers are affected by rounding.

Figure 2-4

This section provides an accounting of the IRRF. For details of other U.S. appropriated funds, donor funds, and Iraqi funds, see Appendices D, E, and F.

IRRF Funds under P.L. 108-106

On November 6, 2003, P.L. 108-106 provided \$18.4 billion for the IRRF to address the extensive Iraq reconstruction requirements identified over the summer and fall of 2003. The act mandates specific sector aid funding totals, with limitations on the transfer of funds between sectors without congressional notification or, in the case of larger modifications, without congressional approval. The act also restricts apportioned funds to five departments or agencies: the Department of Defense (DoD), DoS, USAID, Department of the Treasury (Treasury), and Department of Health and Human Services (HHS).

As of July 6, 2005, these were the IRRF totals:

- \$17.66 billion (95.76%) had been apportioned.
- \$16.66 billion (90.37%) had been committed.
- \$13.80 billion (74.86%) had been obligated.
- \$6.48 billion (35.14%) had been expended.

Figure 2-5 shows the current totals for the IRRF.

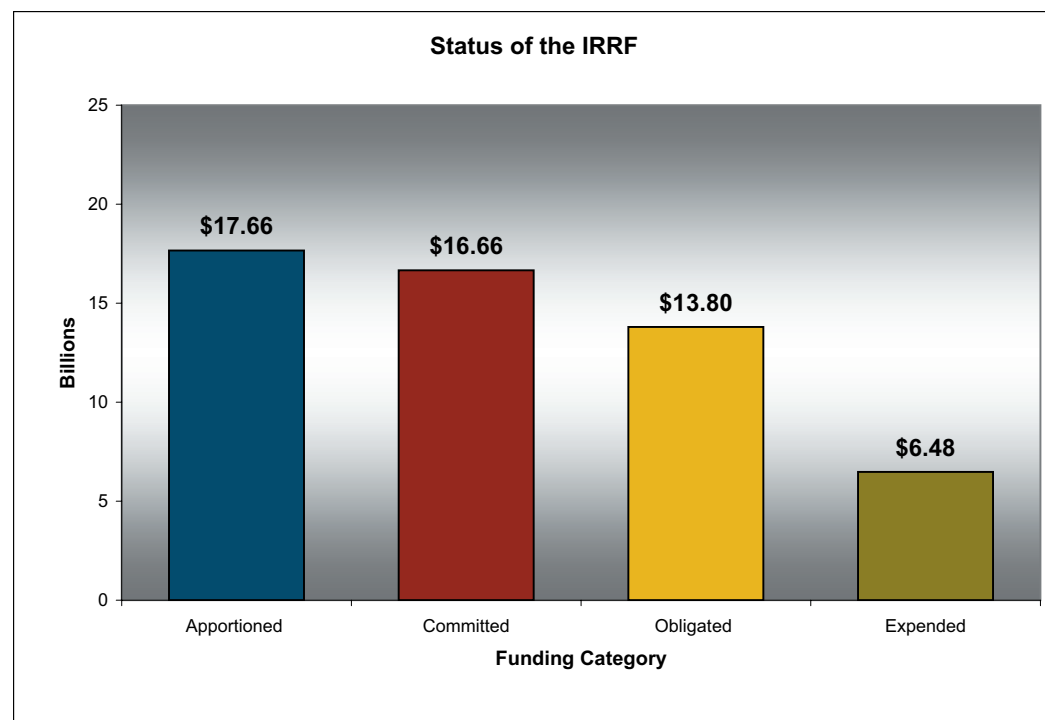


Figure 2-5

Of the \$17.66 billion that has been apportioned, slightly more than \$10 billion of the funds have been apportioned to construction projects, \$6 billion have been apportioned to non-construction projects, and \$0.9 billion have been apportioned for democracy building.

The Office of Management and Budget (OMB) apportioned these IRRF funds:

- DoD, \$12.98 billion (70.39% of the \$18.439 billion total)
- USAID, \$3.10 billion (16.81%)
- DoS, \$1.20 billion (6.51%)
- Treasury, \$390 million (2.12%) (including \$352.7 million in Iraqi debt relief)
- United States Institute of Peace (USIP), \$10 million (.05%)

Figure 2-6 shows how the OMB apportioned IRRF funds.

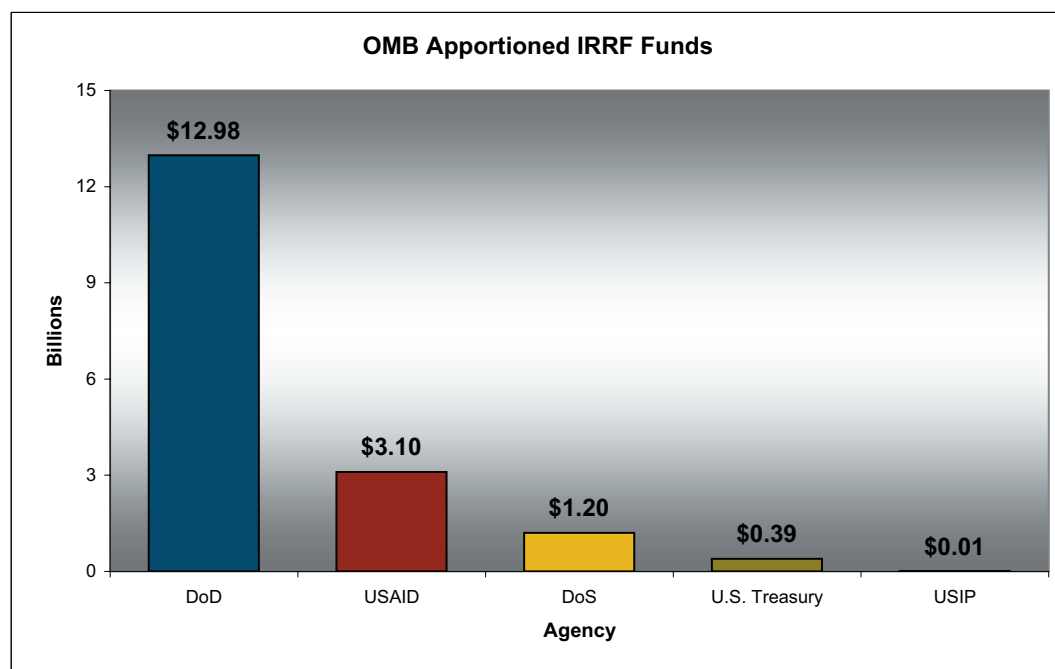


Figure 2-6

Table 2-2 shows the current funding status for the IRRF, with corresponding commitments, obligations, and expenditures.

Appendix D details IRRF apportionments by agency.

IRRF Program Status ^a , as of July 6, 2005 (in millions)					
Sector	2207 Report Spending Plan	Apportioned	Committed	Obligated	Expended
Security & Law Enforcement	\$5,035.6	\$5,035.6	\$4,907.8	\$4,476.4	\$2,853.6
Electric Sector	4,308.2	4,057.6	3,687.1	2,702.5	1,257.6
Water Resources and Sanitation	2,156.7	1,829.2	1,753.7	1,366.5	216.4
Justice, Public Safety, and Civil Society	2,129.5	2,129.5	2,001.6	1,821.4	828.4
Oil Infrastructure	1,723.0	1,723.0	1,599.8	1,126.8	360.6
Private Sector Employment Development	860.3	840.3	834.3	817.5	475.3
Health Care	786.0	786.0	716.7	570.1	128.0
Transportation and Telecommunications Projects	509.0	508.5	480.1	379.6	113.1
Education, Refugees, Human Rights, and Governance	363.0	363.0	324.2	303.8	111.2
Roads, Bridges, and Construction	355.2	355.2	329.9	209.6	106.6
Administrative Expense ^b	213.0	29.0	29.0	29.0	29.0
Total by Sector	\$18,439.5	\$17,656.9	\$16,664.2	\$13,803.2	\$6,479.8
Construction		10,409.9	9,746.5	7,591.2	2,907.5
Non-construction		6,341.7	6,032.8	5,361.7	3,112.7
Democracy		905.3	884.9	850.3	459.6
Total by Program^c	\$18,439.5	\$17,656.9	\$16,664.2	\$13,803.2	\$6,479.8
<p>Note: Data not formally reviewed or audited.</p> <p>^aFigures from DoS Iraq Weekly Update, July 6, 2005.</p> <p>^bIncludes additional \$184M apportioned via 632(a) to DoS D&CP account on June 13, 2005, for follow-on to CPA operating costs, per FY 2004 supplemental language (See Appendix C.) The OMB indicated that this accounting adjustment will be carried across all columns.</p> <p>^cJuly 5, 2005 OMB Reapportionment changes not included in DoS figures.</p>					

Table 2-2

IRRF Spending Changes

Since September 2004, a number of major reallocation efforts have occurred. On September 30, 2004, the first major reallocation shifted \$1.94 billion from the water and sanitation sector and \$1.07 billion from the electricity sector to the security sector (\$1.8 billion), the justice sector (\$461 million), the education sector (\$80 million), and the private employment development sector (\$660 million). An additional \$450 million was reallocated entirely within the oil sector.

In December 2004, an additional \$457 million was reallocated to meet emerging needs in the electrical sector (\$211 million) and to provide post-battle damage reconstruction and rehabilitation in Sadr City, Najaf, Samarra, and Fallujah (\$246 million). In March 2005, an additional \$832 million was reallocated for management initiatives. The management initiatives include money for operations and maintenance programs at various power and water plants, urgent work in the electrical and oil sectors, and cost growth incurred by design build contractors. The DoS July *Section 2207 Report* reallocates \$255 million for Provincial Reconstruction Development Committees, security forces, and election support.

Operating Expenses

Under P.L. 108-106, as amended, the SIGIR is required to report information on the operating expenses funded by the IRRF for U.S. government agencies or departments involved with the reconstruction of Iraq. Table 2-3 provides the status of operating funds derived from the IRRF for each agency with a footprint of operational activities in Iraq. IRRF funds can be provided only to the DoD, DoS, Treasury, USAID, and HHS; therefore, any organization listed outside those departments receives funds through one of those five organizations. This table does not include mission-direct operating expenses. Since the establishment of the U.S. Mission-Iraq and the transfer of governance authority on June 28, 2004, various groups involved with Iraq reconstruction have received support from the budget of the U.S. Mission-Iraq. This support is outside of the SIGIR's IRRF reporting requirements.

Agency-specific IRRF-funded Operating Expenses, as of June 30, 2005 (in millions)						
Agency	FY 2005 Allocated	FY 2005 Obligated	FY 2005 Expended	FY 2004 Allocated	FY 2004 Obligated	FY 2004 Expended
Department of Defense ^a	\$10.235	\$10.235	\$98.362	\$150.54	\$150.54	\$52.617
USACE	\$0.043	\$0.040	\$0.432 ^b	\$12.58	\$9.33	\$6.41
Dept. of Treasury	\$0	\$0	\$0	\$0.78	\$0.00	\$0.20
Dept. of Homeland Security	\$2.950	\$2.483	\$2.483	-	-	-
Dept. of Justice ^c	\$0	\$48.584	\$9.101	\$146.037	\$76.426	\$44.985
Dept. of State ^d	NA	\$3.528	\$1.579	NA	\$2.826	\$2.290
Dept. of Health and Human Services	\$0	\$0	\$0	\$0	\$0	\$0
Dept. of Transportation	\$0	\$0	\$0	\$0	\$0	\$0
Dept. of Commerce	\$0	\$0	\$0	\$0	\$0	\$0
Dept. of Labor	\$0	\$0	\$0	\$0	\$0	\$0
Dept. of Agriculture	\$0	\$0	\$0	\$0	\$0	\$0
	IRRF2 Allocated	IRRF2 Obligated	IRRF2 Expended	IRRF1 Allocated	IRRF1 Obligated	IRRF1 Expended
USAID ^e	\$153.00	\$129.03	\$77.51	\$38.67	\$38.65	\$36.86
<p>Note: This is the exact data as it was received by the SIGIR and has not been formally reviewed, verified, or audited. These operating expenses do not include mission-direct operating expenses.</p> <p>^a DoD FY 2005 operating expense is a building rehab and will be re-classified as a reconstruction asset by 2007.</p> <p>^b FY 2005 expenditures include funds disbursed from FY 2004 obligated.</p> <p>^c DoJ reported its no-year monies in the FY 2004 columns.</p> <p>^d Figures provided for DoS INL only. Allocated figures not available.</p> <p>^e USAID reported information by fund type, not by fiscal year.</p>						

Table 2-3

As the U.S. Mission-Iraq became operational and the Iraq Reconstruction Management Office (IRMO) assumed some of the duties of the CPA, \$105.75 million were transferred from the CPA's P.L. 108-106 appropriation to the DoS to fund these operations. The status of these transferred funds is included in Table 2-4, which is an update of the status of those funds as of June 30, 2005. The Congress also authorized the funding of CPA-IG operations (now the SIGIR) with \$75 million from the 2004 Defense-wide operations and maintenance (O&M) appropriations.

Status of Supplemental Iraq Reconstruction Funding, P.L. 108-106, as of July 6, 2005 (in millions)					
Source	Appropriated	Apportioned	Committed	Obligated	Expended
IRRF2	\$18,439.5	\$17,656.9	\$16,664.2	\$13,803.2	\$6,479.8
CPA-OPS ^b	768.8	768.8	768.8	767.6	694.8
IRMO ^{a,b}	129.5	129.5	105.6	105.6	90.4
SIGIR ^b	75.0	75.0	75.0	29.6	20.2
Total	\$19,412.8	\$18,630.2	\$17,613.6	\$14,706.0	\$7,285.2
Note: Data not formally reviewed or audited.					
^a Numbers as of June 30, 2005					
^b Includes \$23.8 million apportionment for reporting purposes.					

Table 2-4

Measuring Outcomes

Few metrics are reported by reconstruction agencies, and these are usually quantitative. Quantitative metrics are often appropriate for analyzing costs, but periodic reports often cover information only during a short period of time. When possible, quantitative data should be presented over an extended time to provide historical context and allow reviewers to see trends.

While quantitative information is somewhat helpful in understanding commodities like oil or electricity, it does not provide adequate information about more complex sectors, such as health care or justice. In these sectors, qualitative metrics that report on quality, working state, durability, and sustainability are necessary to understand the value being achieved by reconstruction efforts.

Reconstruction agencies collect some data on planned projects and on estimates of the impact of completed projects, but they report it only to managers of reconstruction organizations. Added detail and historical context in summary reports, such as the DoS *Iraq Weekly Status*, would provide a more useful guide to the weekly progress of reconstruction.

To help complete the picture of U.S. Iraq reconstruction efforts, the SIGIR follows a few key metrics over time and presents them in their historical context in the Quarterly Reports. No attempt has been made to verify the validity of the data at this time.

Employment Data

In its *Iraq Weekly Status* reports, the DoS reports the number of Iraqis employed on projects administered by the U.S. government. These reports typically provide data for the current week and compare this data to the previous week. Figure 2-7 summarizes these weekly Iraqi employment reports, beginning with August 2004.

During April and May 2005, the number of Iraqis employed on U.S. government projects has gradually decreased from its peak of more than 170,000 in mid-March. However, as of June 2005, the number of employed Iraqis has begun to increase to a high of 180,173. This reflects employment only on U.S. government projects; it does not capture jobs associated with U.S. projects transferred to the Iraqi ministries.

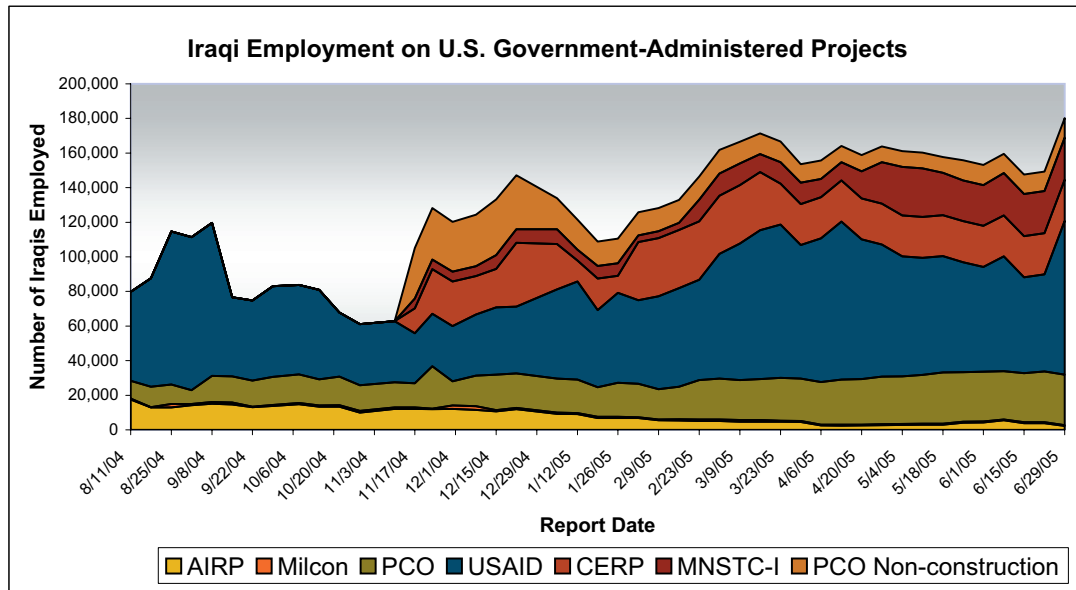


Figure 2-7

Oil

During this reporting period, Iraqi crude oil production continued to fall short of the 2.5 million barrels per day (MBPD) target set by the Iraqi Ministry of Oil. According to DoS *Iraq Weekly Status* reports, production remained stable, around 2.1 MBPD, through June 2005. Figure 2-8 shows Iraq's weekly average oil output since the beginning of 2004.

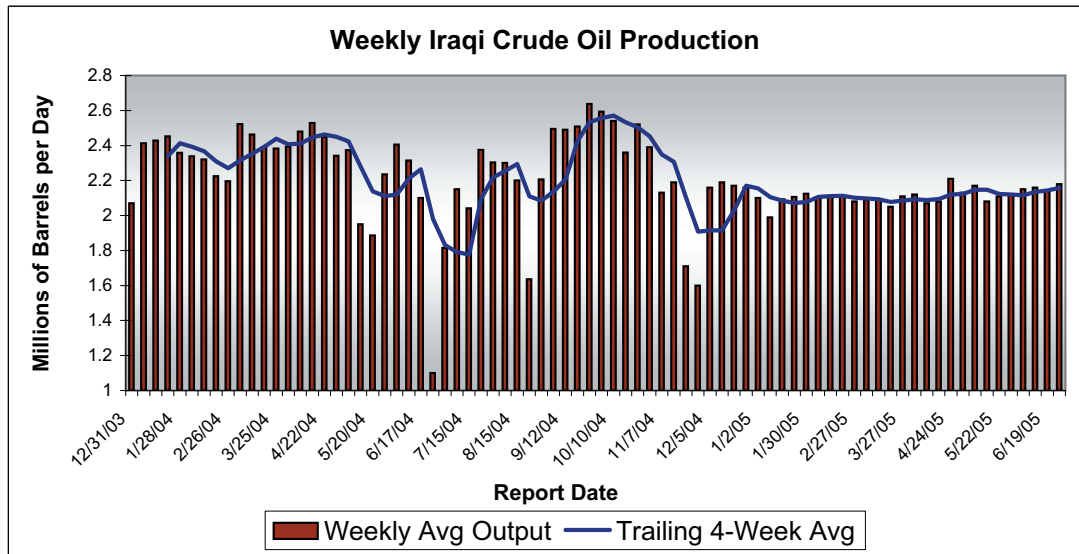


Figure 2-8

Crude Oil Exports

Exporting crude oil is one of Iraq's major sources of income. Crude oil export numbers stayed close to the level of the last reporting period—around 1.3 MBPD—according to the DoS *Iraq Weekly Status* reports. The revenue dropped slightly from the beginning of the quarter to end at \$1.58 billion for June 2005. Figure 2-9 shows Iraq's crude oil export volume and revenues since June 2003.

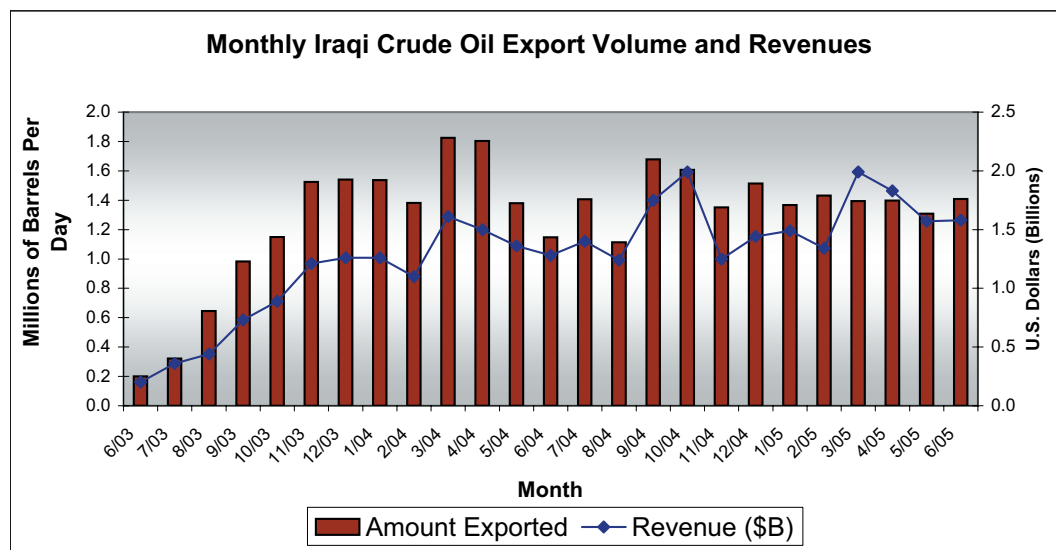


Figure 2-9

Refined Petroleum Supplies

Before it can be burned efficiently, most oil must be refined. Since soon after the war, reconstruction organizations have been reporting on Iraq's nationwide output of refined petroleum products, such as gasoline, diesel, kerosene, and liquid propane gas. During this reporting period, refined petroleum has shown some volatility, but on average, the output level has stayed unchanged. Figures 2-10 and 2-11 show weekly numbers for Iraq's nationwide supplies of refined petroleum as reported in the *Iraq Weekly Status* reports.

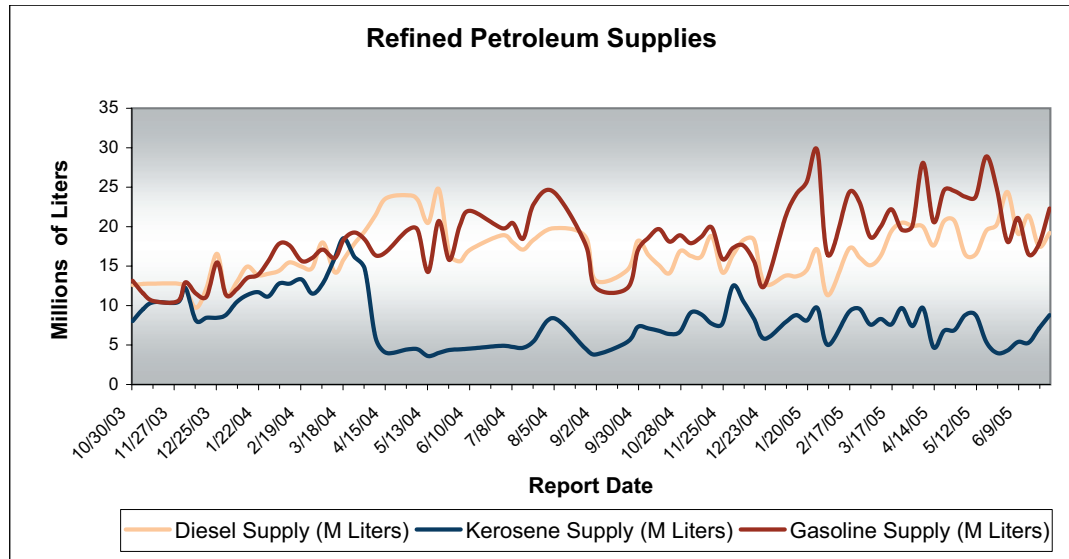


Figure 2-10

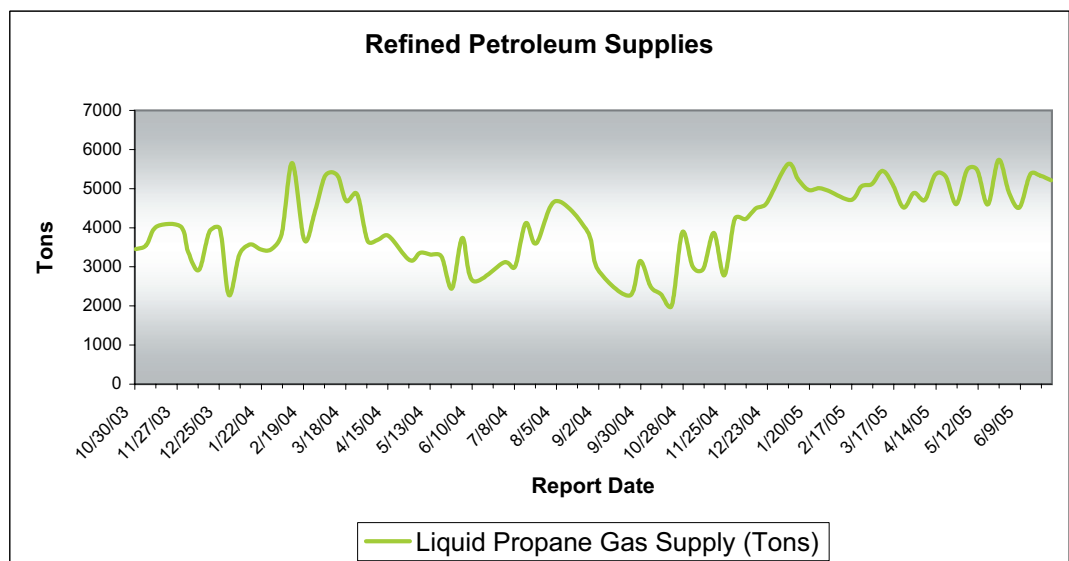


Figure 2-11

Refined Petroleum Stocks

In addition to tracking the supply of refined petroleum products, reconstruction organizations have been reporting on the levels of Iraq's refined petroleum stocks. The goal is to maintain at least a 15-day supply of all refined products at maximum consumption rates. During this reporting period, all four products have attained higher stock levels from March 2005, while liquid propane gas (LPG) passed the 15-day goal with a 17-day stock level. Figure 2-12 shows monthly numbers for Iraq's nationwide stocks of refined petroleum as reported in the *Iraq Weekly Status* reports.

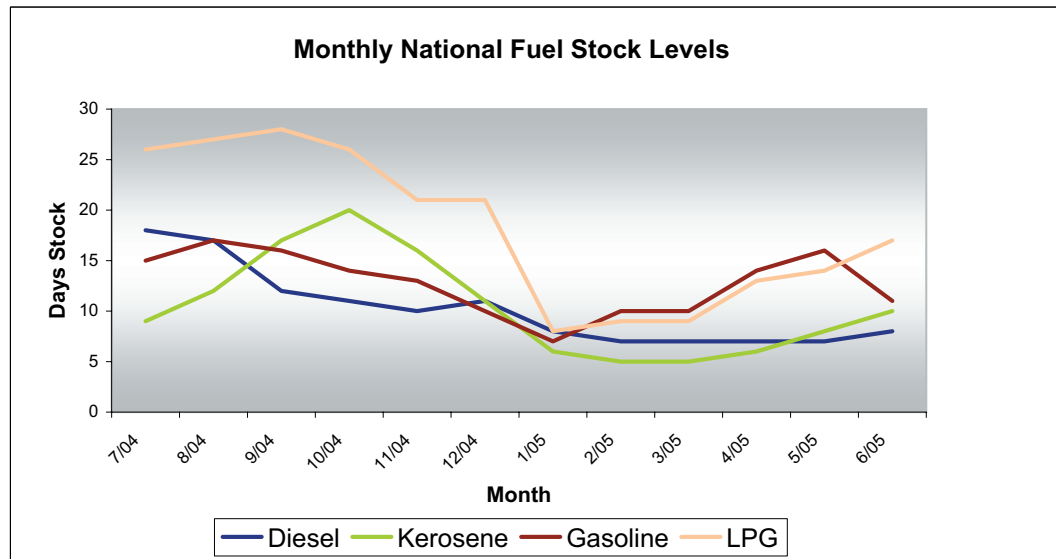


Figure 2-12

Electricity

Electricity supply remains constrained by a lack of generating capacity, fuel shortages at generating plants, a weak distribution system, and an infrastructure that is much more fragile and dilapidated than originally estimated. The electricity load served by the grid has surpassed the pre-war levels of 95,000 megawatt hours (MWh) to reach an all-time high of 108,200 MWh in June 2005, according to the DoS *Iraq Weekly Status* reports. Peak daily generating capacity averaged approximately 4,300 megawatts (MW) during this reporting period and reached a high of 4,888 MW in June 2005. Figure 2-13 shows electricity output in MW and electricity load served in MWh.

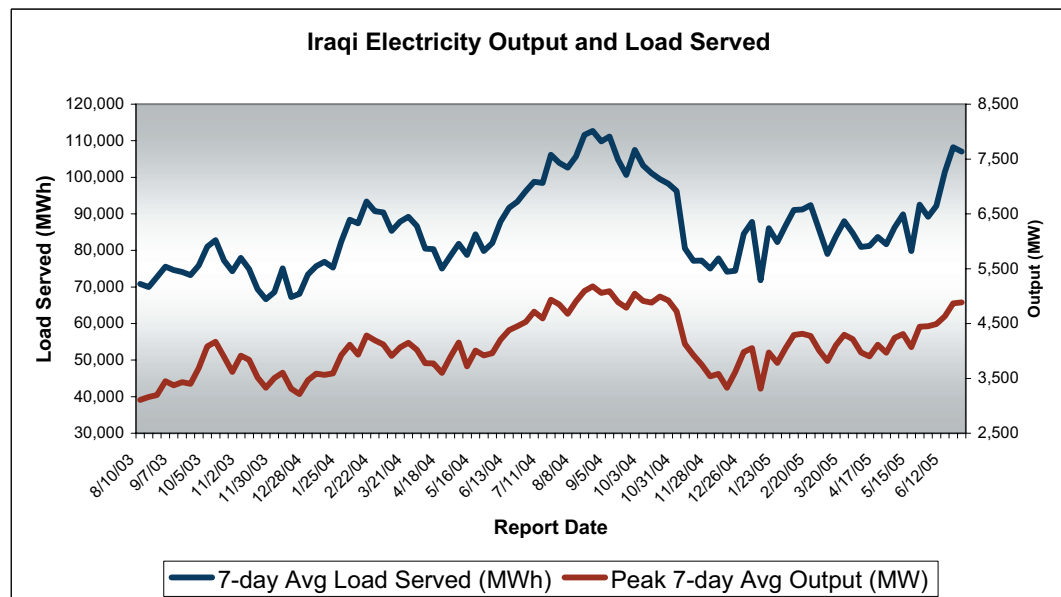


Figure 2-13

Telecommunications

The telecommunications usage reported by reconstruction agencies since the end of the war has continued to grow steadily. Wireless telephone service showed the biggest gains and now has a subscriber base of more than 2,600,000. Landline service has increased at a much slower pace, adding about 15,000 subscribers from the last reporting period, to a new all-time high of 997,675. Figure 2-14 shows weekly snapshots of the numbers of telecommunications subscribers reported in the *Iraq Weekly Status* reports since February 2004.

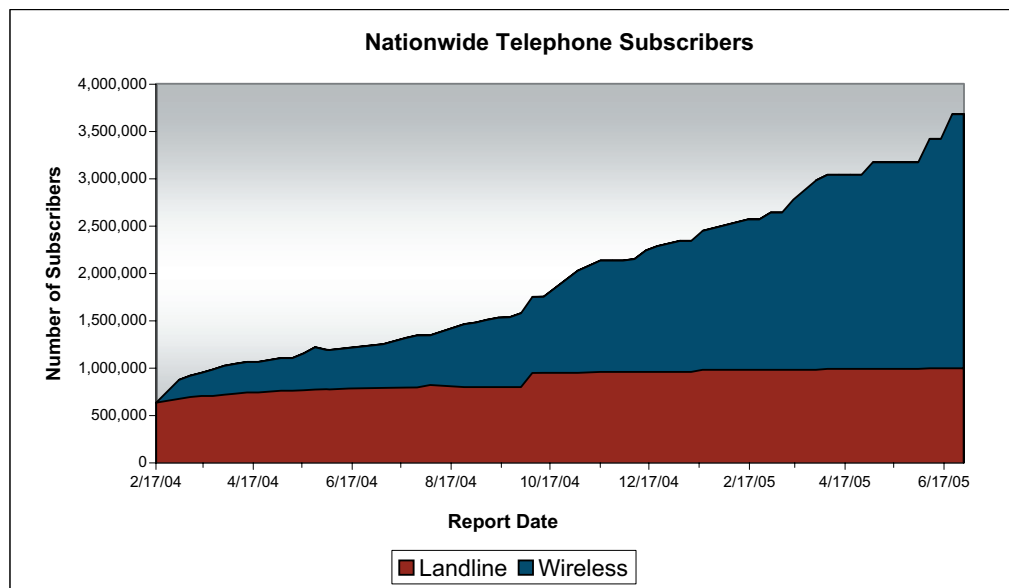


Figure 2-14

Training Iraqi Security Forces

Properly trained and equipped Iraqi security forces will serve an essential role in achieving Iraq's goals for stability. Iraqi security forces are divided into Ministry of Interior forces and Ministry of Defense forces. Ministry of Interior forces include Police and Border Enforcement units, which account for more than 90% of all Ministry of Interior forces, according to the DoS *Iraq Weekly Status* reports. Army, Intervention Force, and former National Guard units contain more than 95% of all Ministry of Defense security personnel.

The number of trained and equipped Iraqi security personnel has grown consistently, reaching an all-time high of 169,812, as of June 2005, according to the DoS *Iraq Weekly Status* report. This is an increase of more than 48% since December 2004, when the total number of trained and equipped security personnel was 114,338. Figure 2-15 shows weekly progression of Iraqi security forces personnel strength reported in the *Iraq Weekly Status* reports since December 2004.

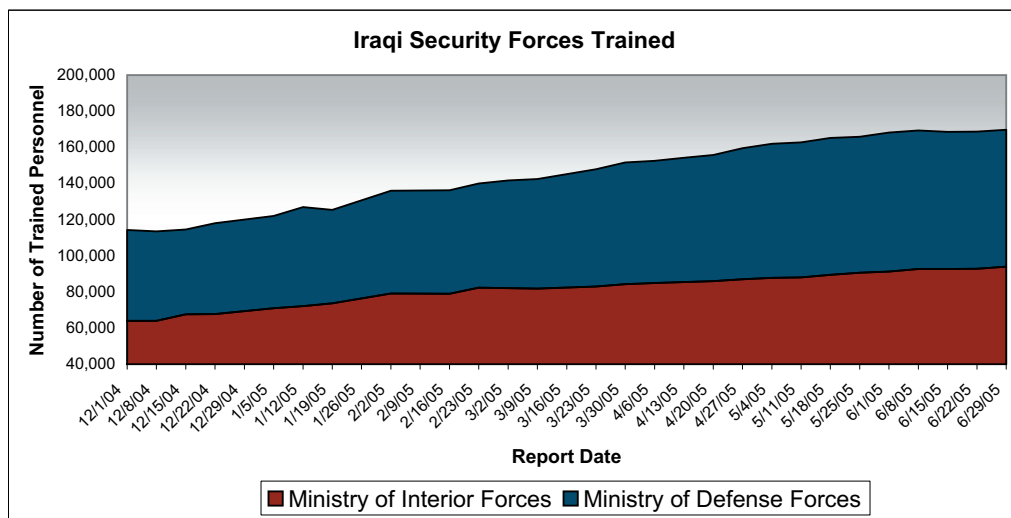


Figure 2-15

Update on Iraqi-U.S. Reconstruction Approach

This quarter, Ambassador Zalmay Khalilzad was appointed the new ambassador to Iraq. As the ambassador to Afghanistan, Ambassador Khalilzad led the reconstruction efforts in that country. His stated approach to his new post will involve extensive engagement of Iraqi leadership, particularly during the drafting of a unifying national constitution this fall¹¹. He is also moving to decentralize reconstruction activities and engage Iraqi planners more fully into the process.

As part of the emphasis on regional input, the U.S. Embassy-Iraq asked the SIGIR to assist the Provincial Reconstruction Development Committee Initiative as an advisor to the Provincial Support Team. This initiative, developed to encourage greater interaction among Iraqi government officials, focuses on the local communities and governance. As this initiative moves forward, the SIGIR will provide advice on accountability and management control issues.

Planning Minister Barham Salih recently announced a number of new initiatives that complement this approach by U.S. Embassy-Iraq. These new initiatives signal a commitment to the development of a National Development Strategy (NDS)¹². This National Development Strategy, presented to the Iraq Donor Conference in Jordan on July 18, 2005, is an overarching framework for government reconstruction and development policy¹³.

Further Reading

For more details on Iraq reconstruction activities, see the DoS July 2005 *Section 2207 Report*. This report and the *Section 2207 Reports* beginning in October 2004 can be found at: <http://www.state.gov/p/nea/rls/rpt/2207/>

Section 2207 Reports until July 2004 are archived by the Office of Management and Budget at: <http://www.whitehouse.gov/omb/legislative/>

The DoS *Iraq Weekly Status* reports can be found on the Web at: <http://defendamerica.mil>

The USAID posts its weekly updates on Iraq reconstruction at: <http://www.usaid.gov/iraq/>

The PCO posts updates on construction starts and Iraqi employment at: <http://www.rebuilding-iraq.net/>

Transcripts of Pentagon press interviews with Iraq reconstruction officials are available on the Web at: <http://www.defenselink.mil/transcripts/>



TREATMENT FACILITY INSPECTION – An engineer and auditor from a Special Inspector General for Iraq Reconstruction (SIGIR) assessment team inspect a settling tank at a central Iraq water treatment plant.

Section 3

Public Law 108-106 (P.L. 108-106), as amended, requires the Special Inspector General for Iraq Reconstruction (SIGIR) to report to the Congress quarterly on the progress of its activity. This section provides updates on:

- SIGIR Mission and Duties
- SIGIR Audits
- SIGIR Investigations
- SIGIR Project Assessment Program
- SIGIR Hotline
- Other SIGIR Activities and Initiatives
- SIGIR Website

More information about the SIGIR's oversight activities is available at www.sigir.mil.

SIGIR Mission and Duties

The SIGIR is the successor to the Coalition Provisional Authority Inspector General (CPA-IG), which began operations in late January 2004 under P.L. 108-106. The re-designation and modification of authorities of the CPA-IG were enacted in P.L. 108-375 on October 29, 2004.

The CPA-IG's oversight covered:

- the activities of the Coalition Provisional Authority
- the Development Fund for Iraq (DFI), which in mid-2004 comprised approximately \$22 billion in Iraqi oil revenues, as well as seized and vested funds
- the \$18.4 billion Iraq Relief and Reconstruction Fund (IRRF) in U.S. taxpayer dollars

When the Congress re-designated the CPA-IG as the SIGIR, the organization retained most of the IG's oversight authority, but reduced the oversight charter with respect to the DFI.

The SIGIR is a unique organization within the inspector general community and reports directly to the Secretaries of Defense and State. A temporary organization with budgetary independence and a narrowly focused mission, the SIGIR provides most of the oversight of the IRRF. The SIGIR provides quarterly reports to the Congress about issues and deficiencies related to Iraq reconstruction programs and operations and recommends corrective actions.

P.L. 108-106, as amended by P.L. 108-375, and the Inspector General Act of 1978 outline the duties of the SIGIR:

- Provide for the independent and objective conduct and supervision of audits and investigations of the programs and operations funded by the IRRF.
- Provide for the independent and objective leadership and coordination of, and recommendations on, policies designed to promote economy, efficiency, and effectiveness in the administration of the programs and operations funded with amounts appropriated or otherwise made available to the IRRF.
- Prevent and detect fraud, waste, and abuse.
- Review relevant existing and proposed legislation and regulations and make appropriate recommendations.
- Maintain effective working relationships with other federal, state, and local governmental agencies, and non-governmental entities regarding the mandated duties of the SIGIR.

- Inform the Congress and the Secretaries of State and Defense of the necessity for and progress of corrective action.
- Comply with the audit standards of the Comptroller General, and avoid duplication of Government Accountability Office (GAO) activities.
- Report violations of federal criminal law to the U.S. Attorney General and report on the prosecutions and convictions that have resulted.
- Maintain records on the use of IRRF funds to facilitate future audits and investigations of the use of such funds.
- Submit reports (Quarterly and Semiannual) to the Congress.

The SIGIR's statutory charter is available at <http://www.sigir.mil/laws.html>.

Operational Agreements

On June 6, 2005, the SIGIR concluded a Memorandum of Understanding (MOU) with the Secretary of the Army to ensure the effective conduct and supervision of audits and investigations relating to U.S. Army programs and projects funded by the IRRF. This MOU defines the areas of coordination and cooperation between the SIGIR and the Department of the Army and also establishes areas of support for the SIGIR. The MOU is provided in Appendix G.

Legislation and Regulations

The Inspector General Act of 1978 [Section 4(a)(2)], which was applied to the SIGIR by P.L. 108-106, as amended, requires the SIGIR to:

“review existing and proposed legislation and regulations relating to programs and operations of the office and to make recommendations in the semiannual reports...concerning the impact of such legislation or regulations on the economy and efficiency in the administration of programs and operations administered or financed by such establishment or the prevention and detection of fraud and abuse in such programs and operations.”

Legislation

Amendment to FY 2006 Foreign Operations Appropriations Bill

The SIGIR noted that on July 20, 2005, the Senate passed the FY 2006 Foreign Operations appropriations bill (H.R. 3057) containing an amendment that would extend the mandate of the SIGIR and provide additional operating funds. The measure, co-sponsored by Senators Russ Feingold and Susan Collins, would change the formula for the termination of the SIGIR, which is currently 10 months after 80% of the IRRF has been obligated. The new language would change the word “obligated” to “expended.” The measure also authorizes \$30 million of funds from the IRRF to be used for extended SIGIR operations in FY 2006. Enactment of this measure would ensure that SIGIR

oversight activities could continue beyond the currently projected termination of spring 2006.

Other Legislation

During the appropriations process, the 109th Congress considered several legislative actions that could affect Iraq reconstruction. If passed into law, these initiatives would complete the final round of debt relief for Iraq and transfer \$150 million from the IRRF to U.S. operations in the Sudan. Also, the United States Agency for International Development (USAID) proposed \$451 million in new funding for Iraq reconstruction. The House Appropriations Foreign Operations subcommittee did not object to this. The subcommittee decided, however, not to raise new funds to support the initiative, leaving open the possibility that the USAID could reprogram existing IRRF funds.

Other legislation that could have an indirect effect on Iraq reconstruction included an unapproved measure that would direct the Department of Defense (DoD) to:

- create new spending guidelines for the Commanders' Emergency Response Program (CERP) funds in Iraq and elsewhere by December 2005
- produce a new Lessons Learned on Iraqi contracting by April 2006

Hearings

On June 21, 2005, the SIGIR presented and submitted testimony at a hearing convened by the House Government Reform Subcommittee on National Security, Emerging Threats and International Relations: *The Development Fund for Iraq: U.S. Management of Iraqi Oil Proceeds and Compliance with U.N. Security Council Resolution 1483*.

The SIGIR's testimony is provided in Appendix H.

Regulations

During the six-month period ending June 30, 2005, no new regulatory action affected the SIGIR.

SIGIR Audits

The SIGIR conducts audits to carry out its mission to promote economy, efficiency, and effectiveness in the administration of programs and operations funded with amounts appropriated or otherwise made available to the IRRF and to detect and prevent waste, fraud, and abuse.

The scope of the SIGIR audits includes:

- performing oversight and accounting of the obligation and expenditure of such funds
- monitoring and reviewing reconstruction activities funded by such funds
- monitoring and reviewing contracts funded by such funds
- monitoring and reviewing the transfer of such funds and associated information between and among departments, agencies, and entities of the United States and private, non-governmental entities
- maintaining records on the use of such funds to facilitate future audits

To meet its mandate, the SIGIR maintains a staff of professional auditors appointed in the excepted service, detailed from federal government agencies, and selected from the private sector. The SIGIR auditors have a solid background in performance auditing. The audit staff also has available for assistance, when necessary, a specialized technical assessment team. The SIGIR's ongoing recruitment initiatives continue to enhance and increase auditing coverage with more staff who are familiar with the policies, procedures, contracts, and systems in use in Iraq.

Since its April 2005 Report to Congress, the SIGIR has issued five final reports of audits addressing operational and financial controls and procedures. Nine audits are in process. The SIGIR discontinued two audits during this reporting period. Current and future audits address the SIGIR 2005-2006 Audit Plan objectives. The full text of the Audit Plan can be found at the SIGIR Website: http://www.sigir.mil/pdf/Audit_Plan_Feb_2005E.pdf.

All audit work is performed in accordance with generally accepted government auditing standards prescribed by the U.S. Comptroller General. During the next quarter, the SIGIR will implement an audit follow-up program to determine whether previous significant findings and recommendations have been addressed by the management of the audited entities.

Completed Audit Products

The SIGIR completed five audit products since the April 30, 2005 Report. Table 3-1 lists the audit products completed from January 31, 2005 to July 31, 2005. The full text of all completed SIGIR audit products can be found at the SIGIR Website: http://www.sigir.mil/audit_reports.html.

Completed SIGIR Audit Products, since January 31, 2005						
	Report Number	Report Title	Date Issued	Recommendations		
				Total	Closed	Open
1	05-001-T	The Development Fund for Iraq - Testimony Before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives	June 21, 2005	0	-	-
2	05-005	Compliance with Contract No. W911SO-04-C-0003 Awarded to Aegis Defence Services Limited	April 20, 2005	7	-	7
3	05-006	Control of Cash Provided to South-Central Iraq	April 30, 2005	8	-	8
4	05-007	Administration of Iraq Relief and Reconstruction Fund Contract Files	April 30, 2005	7	-	7
5	05-008	Administration of Contracts Funded by the Development Fund for Iraq	April 30, 2005	6	-	6
6	05-009	Reconciliation of Reporting Differences of the Source of Funds Used on Contracts After June 28, 2004	July 8, 2005	0	-	-
7	05-010	Interim Briefing to the Project and Contracting Office and the Joint Contracting Command - Iraq on Award Fee Process	July 26, 2005	5	-	5
8	05-011	Cost-to-Complete Estimates and Financial Reporting for the Management of the Iraq Relief and Reconstruction Fund	July 26, 2005	5	-	5
9	05-012	Policies and Procedures Used for Iraq Relief and Reconstruction Fund Project Management – Construction Quality Assurance	July 22, 2005	0	-	-

Table 3-1

Testimony: The Development Fund for Iraq

Report No. 05-001-T, issued June 21, 2005

Stuart W. Bowen, Jr., Special Inspector General for Iraq Reconstruction, submitted and presented testimony before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives, regarding the matter of the

Development Fund for Iraq and its management by the United States. The full text can be found in Appendix H.

Reconciliation of Reporting Differences of the Source of Funds Used on Contracts After June 28, 2004

Report No. 05-009, issued July 8, 2005

The overall objective of this audit was to determine whether contracts awarded after June 28, 2004, and identified as funded by the Development Fund for Iraq (DFI), were actually funded by the DFI or were instead funded by the Iraq Relief and Reconstruction Fund (IRRF). A secondary objective was to report to the fund managers the necessary actions that may be needed to correct the obligation amounts, the current data files, and other actions as appropriate. However, during the course of this audit, the SIGIR found that it could not fully address the overall objective because 21 of the 69 contracts identified for review could not be located by government officials.

The SIGIR concluded that the 48 contracts reviewed disclosed no instances of incorrect obligations of DFI funds. In 39 contracts, the obligations of DFI occurred before June 28, 2004. Obligations for the remaining nine contracts did not cite DFI funds but rather U.S. funds appropriated by the Congress. The obligation documents for the six contracts identified as the Multi-National Corps-Iraq cited Commanders' Emergency Response Program funds, and the other three contracts cited the IRRF as the source of the funding.

The SIGIR also concluded that the Joint Contracting Command-Iraq (JCC-I) current contract data files were not accurate and not adequately supported. Our review showed that 48 of the 69 contracts contained data entry errors in documenting the date of the contract award or the source of the funding.

The JCC-I officials stated that the 21 contracts that could not be located may have been destroyed by a rocket that struck the Presidential Palace in January 2005 or that some of these contracts were turned over to Iraqi ministry officials after contract completion and final review by contracting officials. However, the JCC-I had no records to support these conjectures.

During the audit, the JCC-I corrected the Contract Management Information System reporting errors identified by the audit. The SIGIR believes that these actions sufficiently corrected the identified deficiencies. The SIGIR did not make any recommendations in this report because recommendations were previously made to the JCC-I to improve contract file data management¹⁴.

Interim Briefing to the Project and Contracting Office and the Joint Contracting Command-Iraq on Award Fee Process

Report No. 05-010, issued July 26, 2005

The overall objective of the audit was to determine whether award fees are adequately reviewed, properly approved, and awarded by the Project and Contracting Office-Iraq (PCO) according to established standards. Specifically, the SIGIR was to determine whether:

- an Award Fee Evaluation Board (AFEB) and pertinent policies and adequate procedures have been established and consistently applied to the evaluation of award fees
- award fee plans clearly identify the specific award fee evaluation criteria for assessing contractor performance and determining the amount of the award fee:
 - The performance indicators were properly established.
 - The performance requirements were properly defined.
- AFEB recommendations are supported by appropriate evaluations of contractor performance
- the Award Fee determination is documented in sufficient detail to show that the integrity of the award fee determination process has been maintained

The SIGIR reviewed 18 cost-plus-award fee contracts, valued at about \$6.9 billion. Although the PCO and the Joint Contracting Command-Iraq (JCC-I) had established an award fee evaluation board, policies, and procedures, there were a number of inconsistencies in the application of the policies and procedures. Specifically:

- Documentation could not be located for the appointment of the Award Fee Evaluation Chairperson, board members, or performance monitors in all of the contracts.
- Limited evidence was found supporting that the monthly contract assessments are performed.
- Self-assessments from contractors were not always in the file.

In addition, PCO and JCC-I did not clearly identify the specific award fee evaluation criteria or define performance indicators or metrics. Further, the Award Fee Plan did not provide incentives for the contractor to strive for quality efforts toward a superior performance.

Although the SIGIR found that PCO and JCC-I have taken steps to improve its award fee process, opportunities still exist to improve the award fee plans to more clearly identify the specific award fee evaluation criteria and to modify the methodology of applying the award fee to provide additional incentive for contractors to achieve quality results.

This interim briefing contained five recommendations. As agreed at the briefing, both the PCO and JCC-I management officials provided oral comments. In summary, officials of both activities agreed with the SIGIR's recommendations to improve documentation, and stated that they are already taking many additional actions to improve the documentation of the award fee process and files. They also provided a draft of a new policy and procedure document for the award fee process. However, both the Project and Contracting Office and Joint Contracting Command officials stated that they are going to assess the impact of the recommendation for changing the award fee methodology on the basis of how contractors are currently awarded fees. They requested an opportunity to complete their impact assessments and brief the SIGIR on their results prior to the completion of our ongoing audit in this area. The SIGIR agreed.

Cost-to-Complete Estimates and Financial Reporting for the Management of the Iraq Relief and Reconstruction Fund

Report No. 05-011, issued July 26, 2005

The objective of this initial segment of the overall audit was to determine whether those information systems used by the Iraq Reconstruction Management Office (IRMO) and the Project and Contracting Office (PCO) to monitor Iraq Relief and Reconstruction Fund (IRRF) funds were adequately reliable and sufficiently coordinated among those organizations to ensure the accurate, complete, and timely reporting to senior government officials and the Congress on the use of IRRF funds.

The Section 2207 Report on Iraq Relief and Reconstruction (*Section 2207 Report*) for April 2005, compiled by the IRMO, did not meet the congressionally mandated requirement to include estimates, on a project-by-project basis, of the costs required to complete each project. As a result, without current and accurate cost-to-complete data, the funds available for the completion of the IRRF program cannot be determined and the availability of funds for the initiation of new projects cannot be projected. Inaccurate cost-to-complete estimates could result in needed projects being delayed or not built.

The accuracy of the \$7.9 billion of Department of Defense obligations reported in the Secretary of the Army Report issued March 27, 2005, and the Section 2207 Report for April 2005 could not be verified. This is the source of the DoD information that is incorporated into the Section 2207 Report, consolidating Department of Defense financial reporting of IRRF funds. The transactional data that was provided to the SIGIR as the support for the obligations reported in the Secretary of the Army Report for the SIGIR's review was not reconcilable and consequently did not meet the SIGIR's objectives. The SIGIR subsequently learned, in conversations with PCO, that the information provided to the SIGIR by PCO was not the correct detail information from which the SIGIR could reconcile detail transactions to the Secretary of the Army Report. The SIGIR also learned that the information in this report is not validated for accuracy since it is a compilation of data from various sources.

During the audit, IRMO officials initiated procedures for preparing and reporting cost-to-complete estimates. The IRMO Chief of Staff advised the SIGIR on June 7, 2005, that IRMO will begin reporting cost-to-complete estimates in the *Section 2207 Report* for September 2005. On June 10, 2005, PCO officials began reporting cost-to-complete estimates to IRMO. The SIGIR was advised by the PCO Chief Information Officer and Director of Information Technology that the U.S. Army Corps of Engineers is developing an interface that will link the PCO Oracle Project Accounting interface with the CEFMS database. This is to provide integration of financial and project data that will improve PCO abilities to generate cost-to-complete estimates. The estimated completion date for the interface is August 31, 2005.

The report contained three recommendations to PCO, two concerning cost to complete and one recommendation on ensuring that the PCO data reported to Congress is accurate. PCO concurred with the SIGIR's recommendations concerning cost to complete and are in process of implementing the SIGIR's recommendations. PCO did not concur with the SIGIR's recommendation that PCO certify the information that they present in the Secretary of the Army report. The SIGIR agrees, however, the SIGIR's intention was not for PCO to ensure the accuracy of all the data they compile but each agency that provides this data to PCO should have management controls in place to be able to validate the accuracy of this data. The SIGIR has modified the SIGIR's report to allay PCO's concerns.

The report also included two recommendations to IRMO. IRMO concurred with both of the SIGIR's recommendations. The first recommendation on including the cost to complete information in its 2207 report to the Department of State, IRMO said they concurred as long as they could include the cost to complete information as a separate report with its 2207 submittal due to the sensitivity of the detail information on projects. The SIGIR agreed. On the second recommendation IRMO said the data provided to them does not have to be certified but verified in regards to its accuracy. The SIGIR agreed and made this change in our report.

The SIGIR plans to perform follow-up audits of the estimates of cost-to-complete prepared by the PCO, as well as follow-up audits on the accuracy of the data reported in the Secretary of the Army Report and the Section 2207 Report, and on management controls over the data reported.

The SIGIR plans to perform follow-up audits of the estimates of cost to complete prepared by the PCO, as well as follow-up audits on the accuracy of the data reported in the *Secretary of the Army Report* and the *Section 2207 Report*, and on management controls over the data reported.

Policies and Procedures Used for Iraq Relief and Reconstruction Fund Project Management—Construction Quality Assurance
Report No. 05-012, issued July 22, 2005

The overall objective of this audit was to identify the policies, procedures, and internal controls established by U.S. government organizations for monitoring and reviewing Iraq reconstruction projects.

This information was obtained as part of a broader review of the effectiveness of the U.S. government's policies, procedures, and internal controls, and whether those policies and procedures, and internal controls are adequately coordinated by and among U.S. government organizations and sufficiently consistent for the effective management and timely completion of Iraq reconstruction projects. The SIGIR plans to conduct additional reviews to determine the effectiveness of these policies and procedures and the adequacy of their coordination.

For this audit, the Project and Contracting Office and the U.S. Army Corps of Engineers, the two major organizations involved in Iraq Relief and Reconstruction Fund (IRRF) projects, have established written policies and procedures for establishing and managing construction quality management programs for projects managed and funded by the IRRF.

This report did not contain recommendations; therefore, no management response to this report was required.

Draft Reports Issued

The SIGIR has no draft audits as of the reporting date.

Current Audits

Currently, the SIGIR has nine ongoing audits. Multiple reports will be issued within each audit series.

Cash Controls over Disbursing Officers in Southern Iraq (Project No. D2004-DCPAAF-0034)

The overall objective of this audit series is to determine whether disbursing officers in selected locations in southern Iraq complied with applicable guidance and properly controlled and accounted for DFI cash assets and expenditures. Specifically, these audits will determine whether fund agents adequately controlled cash assets, fully accounted for cash assets and expenditures, and properly returned cash assets. These audits will also determine whether expenditures complied with guidance specifying dollar thresholds and allowed uses.

Commanders' Emergency Response Program (CERP)
(Project No. D2005-DCPAAF-0001)

The overall objective of this audit is to evaluate the adequacy of controls over the CERP. Specifically, the audit will determine if fund allocation procedures were adequate, funds were used for intended purposes, and financial records were accurately maintained and supported.

Information Systems Used for the Management of Iraq Relief and Reconstruction Fund Programs
(Project No. D2005-DCPAAI-0004)

The overall objective of this audit series is to determine whether information systems used by U.S. government organizations result in the effective management of IRRF programs. These audits will also determine whether those information systems were adequately reliable and sufficiently coordinated among those organizations to ensure accurate, complete, and timely reporting to senior government officials and the Congress on the use of IRRF funds.

Policies and Procedures Used for Iraq Relief and Reconstruction Fund Project Management
(Project No. D2005-DCPAAP-0005)

The overall objective of this audit series is to determine whether policies, procedures, and internal controls established by U.S. government organizations result in the effective management of Iraq reconstruction projects. These audits will also determine whether those policies, procedures, and internal controls were adequately coordinated among U.S. government organizations and resulted in sufficient consistency among those organizations for the effective management and timely completion of Iraq reconstruction projects.

Controls Over Equipment Acquired by Security Contractors
(Project No. SIGIR-2005-0006)

The overall objective of this audit is to determine whether controls over equipment acquired by security contractors have been established, implemented, and are effective. The audit will examine selected contracts to determine whether requirements for the acquisition of equipment were valid, adequately supported, properly approved, and the equipment was accounted for and safeguarded.

Selected Sector Reconstruction Activities – Electricity, Oil, and Public Works and Water

(Project No. SIGIR-2005-07)

The overall objectives of this audit series are to determine whether selected sector reconstruction contractors are complying with the terms of their contracts or task orders and whether the government representatives are complying with general legislative and regulatory guidance concerning contract administration and financial management. These audits will also evaluate the effectiveness of the monitoring and controls exercised by administrative contract officers.

Selected Accounting and Reporting of the Obligation and Expenditure of Iraq Relief and Reconstruction Fund (IRRF) Funds

(Project No. SIGIR-2005-08)

The overall objective of this audit is to determine whether accounting and reporting IRRF obligations and expenditures are adequate to determine the cost-of-completion of projects currently underway or planned.

Award Fee Process for Contractors Involved in Iraq Reconstruction

(Project No. SIGIR-2005-10)

The overall objective of this audit series is to determine whether award fees are adequately reviewed, properly approved, and awarded according to established standards. Specifically, these audits will determine whether an award review board, pertinent policies, and adequate procedures have been established and consistently applied to the evaluation and disbursement of award fees. In addition, these audits will determine whether:

- The basis for award determinations are adequately documented in the contract files.
- The performance indicators were properly established, and the performance requirements were properly defined.
- Award fee plans clearly identify the specific award fee evaluation criteria for assessing contractor performance and determining the amount of the award fee.
- Award review board recommendations and determinations are supported by appropriate evaluations of contractor performance.
- The award fee determination is documented in sufficient detail to show that the integrity of the award fee determination process has been maintained.

Management of the Transition and Sustainment of Construction and Non-Construction Projects Funded by the Iraq Relief and Reconstruction Fund (IRRF)
(Project No. SIGIR-2005-11)

The overall objective of this audit series is to determine whether the U.S. government organizations responsible for the management of the IRRF have developed and approved plans to fund and support the transition and sustainment of completed construction and non-construction projects by the Iraqi government and its citizens and whether these plans have been implemented at the sector and project level.

Specifically, these audits will determine whether:

- adequate overall plans for the transition and sustainment of construction and non-construction projects have been established by U.S. organizations responsible for the management of the IRRF at the departmental level and at operating agencies located in Iraq
- analyses have been performed to identify the operations and maintenance requirements for the sustainability of completed construction and non-construction projects by the Iraqi government and its citizens
- funding is or will be needed from the Iraqi government to complete the work on construction and non-construction projects that the U.S. government started but is or will be unable to conclude as originally planned
- budgets, funding sources, and detailed transitional guidelines have been established to ensure that adequate training, materials, and supplies are provided to the Iraqi government and its citizens to effectively enable them to perform operations and maintenance on construction and non-construction projects placed under their control
- U.S. government organizations responsible for the management of the IRRF in Iraq have implemented programs to ensure the effective transition and sustainment of completed construction and non-construction projects by the Iraqi government and its citizens

Discontinued Audits

The SIGIR discontinued two audits during this reporting period:

Discontinuation of the Audit of U.S. Army Corps of Engineers (USACE) Indefinite Delivery-Indefinite Quantity (IDIQ) Contracts and/or Construction-Related Services Available for Use or Used by the Coalition Provisional Authority for Iraq Relief and Reconstruction
(Project No. D2004-DCPAAC-0012)

This audit was initiated by the Office of the Inspector General of the Coalition Provisional Authority (CPA-IG), the predecessor organization to the SIGIR, on

April 29, 2004. The overall objective was to determine whether contracts were awarded in compliance with the Federal Acquisition Regulation; whether the use of USACE in award of contracts was reasonable, economical, and efficient; and whether the internal controls are in place to ensure compliance with the original intent of contracts and that task orders conform to contract statements of work.

Audit work was suspended in June 2004 due to other priority tasks. Though efforts were made to resume audit work in September 2004, the CPA-IG was downsizing in anticipation of the then congressionally mandated termination of the CPA-IG on December 28, 2004. Because the CPA-IG was unable to devote the necessary audit resources to this audit at that time, it was again suspended.

Now that this office has been reconstituted as the SIGIR and is nearing full staffing, the SIGIR found that much of the information accumulated for the original audit was dated and, as a result, terminated the audit. The SIGIR will reevaluate the need for the audit in light of the current situation in Iraq and consider including it in future audit planning.

Discontinuation of the Audit of Electrical Transmission and Distribution for the Erbil Governorate under Task Order 003 of Contract Number W914NS-04-D-0010
(Project No. D2004-DCPAAC-0035)

This audit was initiated by the Office of the Inspector General of the Coalition Provisional Authority (CPA IG), the predecessor organization to the SIGIR, on September 24, 2004. The overall objective was to determine whether the contractors for the Erbil Electrical Transmission and Distribution project were complying with the terms of the Task Order, including an evaluation of the effectiveness of the PCO's monitoring and control.

Audit work was suspended in November 2004 due to other priority tasks. In addition, at the time that the audit was suspended, insufficient construction activity had been performed to enable an effective audit.

On May 9, 2005, the SIGIR announced a more encompassing audit of Selected Sector Reconstruction Activities—Electricity, Oil, and Public Works and Water (Project No. SIGIR-2005-07). The objectives of this audit are to determine whether selected sector reconstruction contractors are complying with the terms of their contracts or task orders and whether the government representatives are complying with general legislative and regulatory guidance concerning contract administration and financial management. The audit will also evaluate the effectiveness of the monitoring and controls exercised by administrative contract officers. Because the objectives of this current audit include the objective that was announced for the audit of the Erbil electrical project, the SIGIR terminated the Erbil electrical project audit. The SIGIR will

consider inclusion of this project in the audit of Selected Sector Reconstruction Activities when sufficient work is accomplished on the Erbil electrical project task order to warrant audit.

Future Audits

The SIGIR will conduct performance audits that assess the economy, efficiency, effectiveness, and results of Iraq reconstruction programs and operations. These audits will be accomplished through individual audit projects of specific issues, as well as audit series that will evaluate several components of related topics. For specific details, see the SIGIR 2005-2006 Audit Plan at http://www.sigir.mil/pdf/Audit_Plan_Feb_2005E.pdf.

SIGIR Investigations

In December 2004, the SIGIR began to substantially increase its capacity to conduct criminal investigations. As the organization was recalibrating in light of its statutory extension. The SIGIR recruited white collar and financial crimes investigators with extensive experience in federal agencies, including:

- the Federal Bureau of Investigation
- the Internal Revenue Service
- the U.S. Customs Service
- the Naval Criminal Investigative Service
- the U.S. Department of State Inspector General's Office

During this reporting period, the SIGIR reassigned five investigators to other duties and released four other investigators. Eleven investigators were added, bringing the staffing level to 14, with 2 vacancies yet to be filled.

Of the 14 investigators currently on staff, 10 are assigned to the SIGIR's Baghdad office, and 4 are assigned to the office in Washington, D.C. Investigators in the Baghdad office originate and conduct SIGIR investigations in Iraq. The investigators assigned to the office in Washington, D.C., provide support for investigations by:

- interviewing witnesses and subjects who have returned from Iraq
- reviewing files and records of U.S. departments and agencies
- working with task force partners
- serving subpoenas
- coordinating prosecutions with the Department of Justice

Investigative Activity

The SIGIR continues to work within its jurisdiction to open and investigate cases that affect government operations or those with prosecutorial potential.

The SIGIR has significantly increased its investigator caseload since reporting in April. Figure 3-1 shows new and closed case activity from January to June 2005.

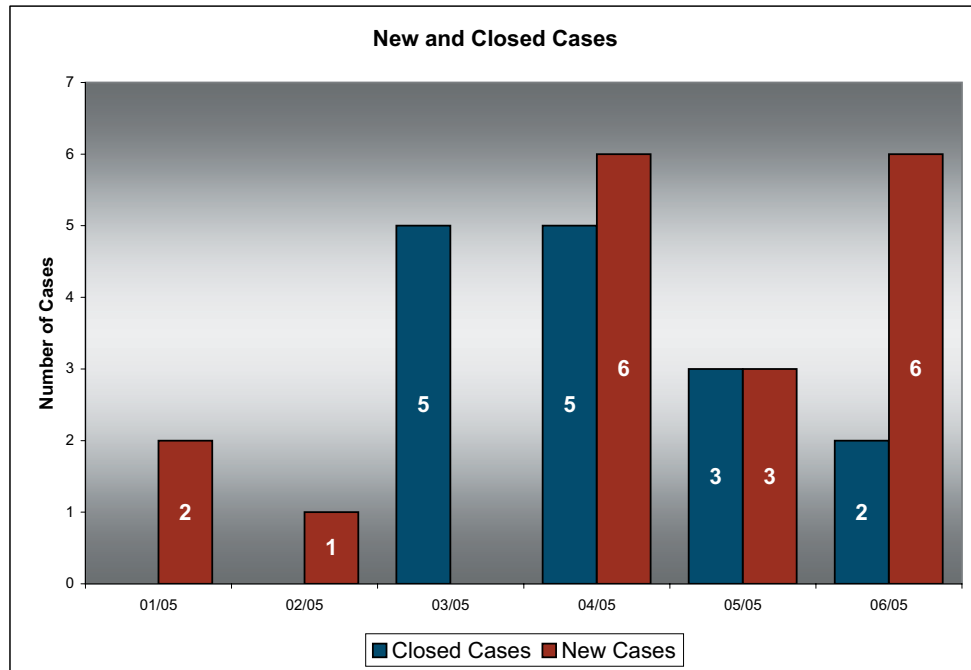


Figure 3-1

Fifteen cases were opened between April and June 2005, compared with three cases opened from January to March 2005. Although 10 cases were closed during this reporting period, the total number of open cases increased to 56. Figure 3-2 shows the number of open cases at the end of each month from January to June 2005.

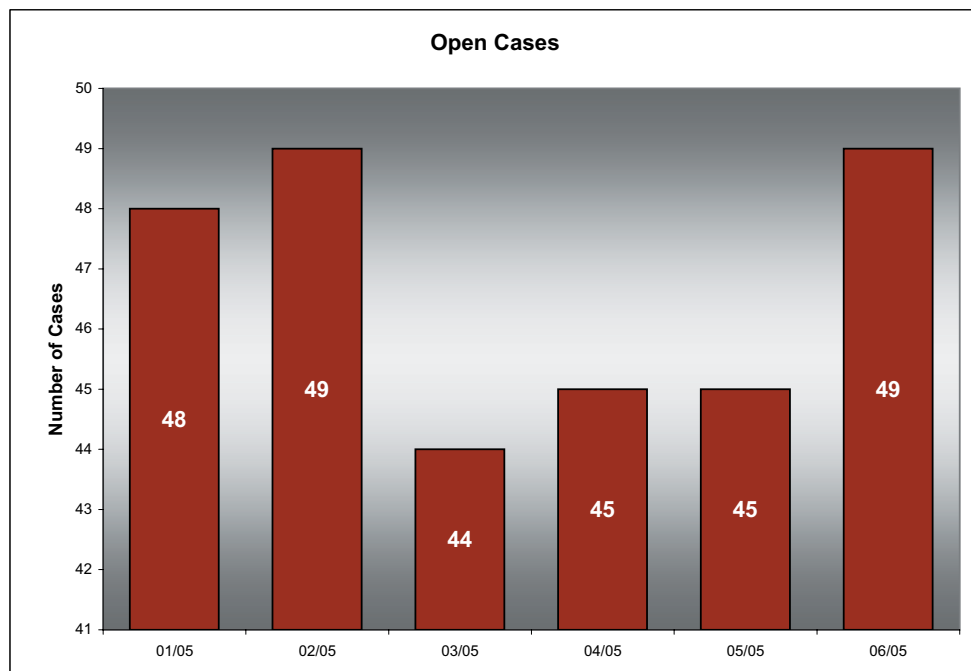


Figure 3-2

Figure 3-3 shows the distribution of the SIGIR's 49 open cases by investigative category.

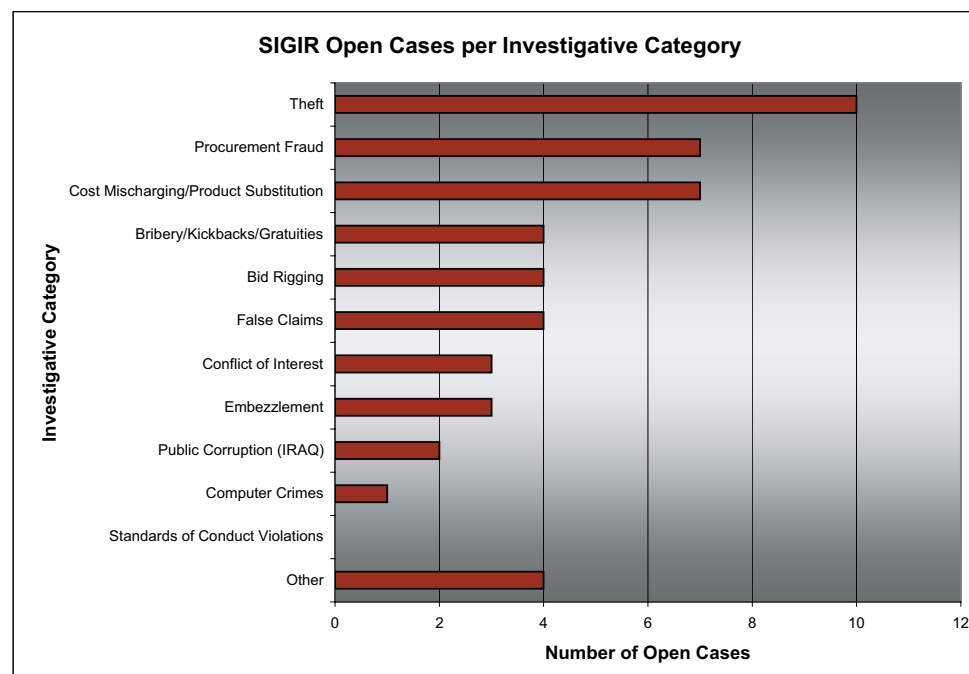


Figure 3-3

Special Investigative Task Force

During this reporting period, the SIGIR created the Special Investigative Task Force for Iraq Reconstruction (SPITFIRE) to enhance its ability to detect fraud, trace international money transactions, and monitor travel. SPITFIRE pursues criminal activity in Iraq reconstruction funding with the specialized resources and abilities of these partners:

- SIGIR
- Immigration and Customs Enforcement, Department of Homeland Security
- U.S. Department of State Office of Inspector General

SPITFIRE employs colocated special agents, the latest electronic databases, and specialized forensic analysis to expeditiously and effectively address these complex investigations.

Working closely with the Money Laundering and Asset Forfeiture Section of the Department of Justice, SPITFIRE is applying a well-recognized and accepted investigative technique to prosecute individuals involved in these crimes and to recover Iraq reconstruction funds that were illegally taken.

Other Investigative Matters

In a *qui tam*¹⁵ False Claims Act (FCA) case, *U.S., ex rel., DRC, Inc. v. Custer Battles, LLC*, two whistleblowers alleged that their former employer, Custer Battles, had submitted tens of millions of dollars of false claims to the Coalition Provisional Authority (CPA). [2005 U.S. Dist. LEXIS 13743 (D. Va., 2005)]

On July 8, 2005, the U.S. District Court for the Eastern District of Virginia issued a ruling on the defendant's motion for summary judgment. This initial decision examined only the threshold question of whether the FCA applies to claims submitted to the CPA. The court focused on whether a "claim" under the FCA requires a demand for payment of U.S. government funds or whether it could also apply to non-U.S. money administered by the U.S. government. The court concluded that there must be a request for U.S. government funds for the FCA to apply. Under this standard, the court ruled that false claims paid with vested¹⁶ or seized¹⁷ funds qualified as a claim under the FCA, but that false claims paid with funds from the DFI¹⁸ do not qualify.

This civil action could be important to subsequent civil actions against companies doing business in Iraq, but should not limit SIGIR investigations and prosecutions. This case is currently isolated to one federal district and narrowly applies to the FCA, which includes specific language requiring presentment of false claims to the U.S. government. The decision does, however, restrict recovery through the FCA. To the extent that such options for recovery are limited by this initial decision, the SIGIR's role in detecting and preventing fraud, waste, and abuse in Iraq reconstruction will be more significant.

SIGIR Project Assessment Program

Mission

During this last quarter, the SIGIR appointed an Assistant Inspector General (AIG) for Special Operations who is in the process of establishing a multi-faceted project assessment program to determine if U.S. taxpayers and Iraqi citizens are getting value for the dollars spent on individual U.S.-funded projects across Iraq. Although SIGIR auditors generally analyze larger programmatic issues and SIGIR investigators focus on significant criminal activities, this new unit focuses on actual work completed at specific projects in Iraq. Team members gather contractual specifications and reported completion information and compare this data to actual on-site efforts and accomplishments.

Approach

The SIGIR is fulfilling this oversight responsibility using both traditional and innovative approaches. A ground assessment team with engineering, audit, and investigative experience was established during this reporting period, which assessed four water projects in central Iraq. Three of the four assessments found significant deficiencies at the sites. The SIGIR expects significant changes in program management by the contractors and management agencies.

The success of this assessment team has prompted the AIG for Special Operations to create two additional ground inspection teams. These teams should begin conducting site assessments during the next reporting period after obtaining additional personnel slots in Iraq from the Department of State and after hiring, training, and equipping additional engineers, auditors, and others.

The AIG for Special Operations is also establishing a small unit that will conduct project assessments using aerial imagery, rather than ground visits. Satellite and other aerial vehicles will be used for this purpose. The SIGIR is working with several other federal agencies to obtain the imagery, imagery analysis capability, and equipment needed for this project. This approach offers many advantages, including:

- *Maximum coverage of projects:* With thousands of projects and limited oversight resources, this approach provides the greatest degree of coverage of projects.
- *Ability to triage high-risk targets:* The approach allows the SIGIR to allocate personnel assets to projects that are most likely encountering issues.

- *Lowest personal risk to SIGIR personnel:* Because of the unstable security situation throughout Iraq, this program minimizes the amount of in-country travel required of SIGIR staff.
- *Lowered threat to on-site/Iraqi contractors/subcontractors:* Minimizing the number of highly visible visits to the project sites—supported by military convoys—minimizes the risk to contractors and subcontractors from insurgents.
- *A shareable tool that can be used by management to improve internal controls:* When fully developed, this approach can be used by Iraq reconstruction project managers to keep watch over programs that they are unable to visit on a frequent basis.
- *Creative leveraging of existing technological capability in theater:* The technology to do this is already in place for the military, and excess unused capacity is now put to good use in safeguarding taxpayer dollars and ensuring results.

Planning

The SIGIR plans to establish as active an assessment program of individual projects across Iraq as our resources will allow. The SIGIR will assess a cross-section of projects from each of the major sectors, including:

- water, electrical, oil, and building construction projects
- projects involving both large and small investments
- projects of different general contractors
- projects in differing sections of the country
- projects in the programs of each of the major U.S. agencies

The assessments will look at the following issues: the significance of the project; the likelihood that fraud or waste would be identified from an assessment; allegations involving specific project sites, projects, or contractors; and security concerns. Assessments that reveal significant discrepancies or evidence of fraud and waste will be referred to SIGIR audit and/or investigations for further inquiry, follow-up, or referral to various U.S. or non-U.S. management or oversight agencies.

Project Assessment Reports

Our Engineering Assessment Team completed project assessments of the in-process work being performed on four relief and reconstruction projects. The objectives of these projects assessments were to determine whether:

- project results will be consistent with original objectives
- project components were adequately designed before construction or installation

- construction or rehabilitation met the standards of the design
- contractor's quality control plan and the U.S. government's quality assurance program were adequate

The SIGIR discussed the results of these project assessments with the Project and Contracting Office (PCO) and U.S. Army Corps of Engineers (USACE) representatives, who concurred with our findings. Recommendations to address the issues identified in these project assessments will be included in a summary audit report.

Al Wahda Water Treatment Plant, Baghdad, Iraq

Project Assessment Report PA-05-001, issued July 25, 2005

The assessment determined that:

- The stated objective of the Al Wahda Water Treatment Plant (WTP) project will not be met under existing plans. Due to significant reductions in the scope of work being performed under the project, the Al Wahda WTP did not and will not increase the quantity of water to the Iraqi people or elevate the quality of the water to potable standards.
 - For example, rehabilitation of the rapid sand gravity filters and pressure filter system was eliminated from the scope of work for this project. During the site inspection, the Iraqi Plant Manager said that the turbidity (which is a measure of suspended solids in a liquid) of outflow from the filters was equal to that of the inflow, which means that the filter system is not functional.
- In addition, during backwash operations, backwash water should flow to the sludge pit; however, due to poor system operation and possibly faulty valves, some of the backwash water (backwash effluent) gets into the clear well tanks, rendering the water not potable. The clear well tanks are the final storage location of the treated water before chlorination and distribution. The Iraqi Plant Manager said that his customers have sand and sediment in their drinking water.
- The total design package was not adequate to complete all work required for a fully functional water treatment facility. Even if the original scope of work had been completed, the Iraqi Plant Manager cited numerous additional requirements needed to make the Al Wahda WTP fully operational.
- The rehabilitation work on the clarifiers and settling tanks and the chemical building construction met the standards of the design.
- The contractor's quality control plan and the U.S. Government's quality assurance program for this project needed improvement and could be directly linked to insufficient quality control at the Al Wahda WTP. The Government project engineer did not approve invoices or recommend payments to the contractor.

Additionally, the assessment disclosed that information relating to Al Wahda WTP in the Project and Contracting Office (PCO) database needed to be updated. PCO data showed projected total estimated cost as \$8.7 million and that the project was 30% complete. Due to substantial de-scoping, the on-site inspection determined that the Al Wahda WTP project was approximately 70%-80% physically complete and that the actual total cost should be revised substantially lower. Revised cost estimates for the Al Wahda WTP were approximately \$2.2 million.

Al Wathba Water Treatment Plant, Baghdad, Iraq
Project Assessment Report PA-05-002, issued July 25, 2005

The assessment determined that:

- The renovation of the Al Wathba WTP will meet the stated objective of improving the living conditions of citizens living in Baghdad by increasing the quantity of potable water available to them, if design specifications are met.
- The design package was complete and sufficiently specific to construct the required buildings and complete the rehabilitation activities of the Al Wathba WTP.
- The rehabilitation work on the clarifier and settling tanks, the chemical building construction, the administration/laboratory building construction, and pressure building construction meet a substantial portion of the standards of the design. However, the collapse of the train 1 effluent weir wall, poor concrete finishing of the chemical building floor, and corrective actions taken during the interrupted concrete pour are all areas of concern.
- The contractor's quality control plan and the U.S. government's quality assurance program for this project needed improvement and could be directly linked to insufficient quality control at the Al Wathba WTP. No government quality assurance testing has been performed and no future government quality assurance testing was planned. The government project engineer did not approve invoices or recommend payments to the contractor.





Al Wathba Water Treatment Plant: Train 1 settling tank shows a collapsed effluent weir wall

Additionally, the assessment disclosed that information relating to Al Wathba WTP in the PCO database needed to be updated. PCO data showed projected total estimated cost as \$4.7 million. Review of the contract files found that the actual total cost should be revised substantially higher. Revised cost estimates for the Al Wathba WTP were approximately \$11.2 million.

Al Nahrwan Water Supply, Baghdad, Iraq

Project Assessment Report PI-05-003, issued July 30, 2005

The assessment determined that:

- The work performed under this contract for the design and construction of a water pipeline, connection of fifty houses to the new water pipeline, and removal of illegal water connections in the City of Al Nahrwan met the stated objectives.
- The design package was complete and sufficiently specific to install the required water pipe lines and make connections to fifty homes.
- The scheduled on-site inspection could not be conducted due to security concerns. The project assessment for the Al Nahrwan Water Supply Project was based solely on USACE quality assurance reports and photographs, contractor quality control reports, and interviews with the USACE quality assurance representative. It appears that the project was completed to the standards of the design, but this could not be conclusively determined without a site inspection.
- The contractor's quality control plan and the U.S. government's quality assurance program were adequate for this project. Proper documentation by the contractor through daily quality control reports and by the USACE Quality Assurance Representative (QAR) through quality assurance reports ensured that the project was completed on time and within budget. The

USACE QAR was on-site during the critical stages of material inspection and pressure testing.

Al Sumelat Water Network, Baghdad, Iraq

Project Assessment Report PA-05-004, issued July 30, 2005

The assessment determined that:

- The project objectives of installation of an 8,830-meter potable water pipeline from an existing water main to the village of Sumelat, with connections, isolation valves, and tee valves to supply water to the village of Al Sumelat were not being met because of deficiencies in quality control, quality assurance, and design, as well as instances in which work performed was inconsistent with the contract specifications.
- The contractor's design was inconsistent with the requirements of the contract and inadequate for the project. The pipeline route and location of valves and tees were not adequately identified. In addition, design of the pipeline route under structures, such as railroads, roadways, and irrigation canals was incomplete.



- Installed sections of the pipeline were not in compliance with the requirements of the contract. Sand base material was not used in the placement of the pipeline, compacting and final grading was not completed, pressure testing had not been accomplished on any section of the pipeline, and the pipeline was routed around curves without the use of elbow fittings. Additionally, the pipeline was in three unusable segments and had not been connected to the water main.

The contractor had not submitted a quality control plan for this project as required by the contract. The lack of a quality control plan can be directly linked to construction not being completed to the specifications of the contract.

SIGIR Hotline

The SIGIR Hotline facilitates the reporting of fraud, waste, abuse, mismanagement, and reprisal in all programs associated with Iraq reconstruction efforts funded by the American taxpayer. Cases received by the SIGIR Hotline that are not related to the DFI or the IRRF are transferred to the appropriate entity. The SIGIR Hotline receives walk-in, telephone, mail, fax, and online contacts from people in Iraq, the United States, and throughout the world.

During the second quarter of 2005, the SIGIR Hotline relocated to the SIGIR headquarters in Washington, D.C., after being colocated with the Department of Defense Office of the Inspector General (DoD OIG) Hotline. Currently, the Hotline is maintained by four staff members.

Second Quarter Reporting

As of June 30, 2005, the SIGIR Hotline had initiated 400 Hotline cases. A summary of these cases is provided in Table 3-2.

SIGIR Hotline Cases						
SIGIR Hotline	Received		Closed		Ongoing	
Second Quarter	Apr-Jun 2005	Cumulative Total *	Apr-Jun 2005	Cumulative Total *	Apr-Jun 2005	Cumulative Total *
Admin Investigation	6	327	8	74	5	87
Dismiss	0	NA	1	12	0	0
Transfer	7	NA	13	71	0	0
Referral	3	NA	4	50	0	0
Assist	1	NA	6	33	0	0
FOIA	0	4	0	4	0	0
<i>Admin Totals</i>	<i>17</i>	<i>331</i>	<i>32</i>	<i>244</i>	<i>5</i>	<i>87</i>
Criminal Investigations	7	58	4	31	7	27
Audits	2	11	0	7	2	4
Totals	26	400	36	282	14	118
*The cumulative totals cover the period since the SIGIR Hotline began operations—from March 24, 2004, to June 30, 2005. Note: Total cases received may not reflect the sum of the closed and ongoing cases.						

Table 3-2

New Cases

During the calendar quarter, April 1–June 30, 2005, the SIGIR Hotline opened 26 new cases, classified in these categories:

- 9 related to fraud.
- 5 related to waste.
- 4 related to general assistance.
- 2 related to abuse.
- 6 were categorized as “other.”

The SIGIR receives most reports of perceived instances of fraud, waste, abuse, mismanagement, and reprisal by electronic mail. The SIGIR’s 26 new cases were received from these sources:

- 17 by electronic mail
- 3 by conventional mail
- 3 by SIGIR Hotline phone calls
- 3 by transfer from DoD OIG Hotline phone calls

Closed Cases

During the reporting period, 36 cases were closed:

- 13 were closed and transferred to other Inspector General agencies.
- 8 were closed by administrative investigations.
- 6 were closed by assists (requests for information or administrative assistance).
- 4 were closed and referred to non-IG entities.
- 4 were closed by criminal investigations.
- 1 was dismissed for lack of sufficient information.

Of the eight cases closed by administrative investigations, two were substantiated and resolved. Because of insufficient information and the inability to collect additional information, two investigation cases could not be substantiated. Four investigations were closed as unsubstantiated.

Transferred/Referred Cases

Most of the cases that were closed during this reporting period were either transferred to another Inspector General entity or referred to a non-Inspector General entity. Seventeen cases were transferred to these organizations:

- 4 were sent to the Multi-National Force-Iraq OIG.
- 4 were sent to the DoD OIG.

- 2 were sent to the Department of State Anti-terror Unit.
- 1 was sent to the Department of State OIG.
- 1 was sent to the USAID OIG.
- 1 was sent to the Multi-National Corps-Iraq OIG.
- 1 was sent to the Joint Area Support Group-Central Equal Employment Opportunity.
- 1 was sent to the U.S. Army Criminal Investigation Command.
- 1 was sent to the U.S. Army Corps of Engineers OIG.
- 1 was sent to the Iraqi Ministry of Finance OIG.

Other SIGIR Activities and Initiatives

In addition to its investigative and oversight activities, the SIGIR has continued to pursue several activities and initiatives begun by the CPA-IG. Each of these efforts advances the promotion of interagency communication and cooperation and combats fraud, waste, and abuse in the execution of Iraq reconstruction funds.

These SIGIR initiatives and activities include:

- SIGIR Iraq Reconstruction Information System (SIRIS)
- Iraq Inspectors General Council (IIGC)
- Iraq Accountability Working Group (IAWG)
- Iraqi Ministry Inspector General Training
- Security and Insurance Initiative
- Lessons Learned/High-Risk Factors Initiative

Detailed information about these activities and initiatives is available on the SIGIR Website at www.sigir.mil.

SIGIR Iraq Reconstruction Information System (SIRIS)

The SIGIR is developing a reporting tool called SIRIS to act as a repository for project, contract, and financial data on Iraq reconstruction. To date, individual agencies have used independent information systems to track their own project, contract, and disbursement data with varying levels of success. The SIRIS will provide a complete, standardized view of information across all agencies and facilitate oversight of the IRRF.

SIRIS will house several types of data:

- *contracting actions* from either electronically scanned or physical copies of the contract documents
- *disbursing data* from multiple financial systems
- *project data* with cost-to-complete estimates

The SIGIR has initiated a large data-gathering effort, sending a data-call letter to each agency that was apportioned IRRF funds. The letter requested access to project, contract, and disbursement information. This data will enable the SIGIR to double-check the information provided by reconstruction agencies. To date, the SIGIR has entered 2,600 contracting actions, which obligated \$13.7 billion. Of that total, approximately 1,500 contracting actions, valued at \$4.5 billion, obligated IRRF funds. The SIRIS will be a useful tool for oversight analysis of Iraq reconstruction financial information.

Coordinating with Other Oversight Agencies

The SIGIR continues to coordinate oversight activities for Iraq reconstruction programs through the IIGC in Washington, D.C., and the IAWG in Baghdad. For information on the oversight activities of agencies that participate in these groups, see Section 4, Other Agency Oversight.

Iraq Inspectors General Council

Established by the CPA-IG on March 15, 2004, the IIGC provides a forum for discussion and collaboration among the inspectors general and staff of the many agencies that use and oversee the IRRF. At IIGC meetings, representatives from member organizations exchange details of current and planned audits. The SIGIR also updates other organizations on its long-range audit planning and its staffing plans. This helps to identify opportunities for collaboration and to minimize duplication of oversight efforts. Members also share insights into the logistical challenges of performing oversight work in Iraq.

The most recent IIGC meeting was held in Washington, D.C., on May 25, 2005. The SIGIR updated council members regarding its activities in Baghdad, including efforts to gather data on finances, projects, and contracts, and to meet with managers of several of the major reconstruction sectors. The SIGIR also led a discussion of IIGC members' efforts to investigate security costs. In addition, members heard a status update on the progress of the SIRIS. Finally, the SIGIR discussed its request that IIGC members contribute to a Consolidated Audit Plan for Iraq Reconstruction Oversight. By bringing together future audit plans from all members into a single document, the Consolidated Audit Plan would further enhance collaboration and cooperation among the organizations performing oversight of Iraq reconstruction:

- Special Inspector General for Iraq Reconstruction (Chair)
- Department of State Inspector General (Co-Vice Chair)
- Department of Defense Inspector General (Co-Vice Chair)
- Department of the Army Inspector General
- U.S. Agency for International Development Inspector General
- Department of the Treasury Inspector General
- Department of Commerce Inspector General
- Department of Health and Human Services Inspector General
- Defense Contract Audit Agency
- U.S. Army Audit Agency
- Government Accountability Office (Observer Member)
- International Advisory and Monitoring Board (Observer Member)
- U.S. Army Corps of Engineers Chief Audit Executive (Observer Member)

The next meeting of the IIGC is scheduled for August 2005. For information about the audits conducted by IIGC members, see Section 4, Other Agency Oversight.

Iraq Accountability Working Group

The SIGIR formed the IAWG to complement the ongoing coordination provided by the IIGC in Washington, D.C. The IAWG is a forum for the forward-deployed audit staffs of the various federal agencies with audit presence in Iraq to coordinate audits, share data relative to Iraq relief and reconstruction, minimize audit disruption to clients, and avoid duplicative efforts.

During this reporting quarter, the IAWG met on July 20, 2005, in the former Republican Presidential Palace in Baghdad, Iraq.

These organizations attended:

- Special Inspector General for Iraq Reconstruction
- U.S. Agency for International Development, Office of the Inspector General
- Defense Contract Audit Agency
- U.S. Army Corps of Engineers, Gulf Region Division, Internal Review Office
- Iraq Reconstruction Management Office, Audit Liaison to the Commission on Public Integrity
- Project and Contracting Office-Iraq, Audit Liaison

At this meeting of the IAWG, audit representatives from each attending agency briefed each other and held question-and-answer sessions on the objectives, scope, and status of ongoing audits. The objectives, scope, and tentative start dates for planned audits were also briefed by representatives of each attending agency. The SIGIR Assistant Inspector General for Audit briefed attending members on the SIRIS, established for projects, contracts, and task orders awarded using IRRF monies; and the upcoming Lessons Learned series of forums to be held in the Washington, D.C. area.

Supporting Iraqi Anti-corruption Organizations

The SIGIR has continued to support the planning, development, and training of the Iraqi Inspector General (IG) System and maintains a relationship and useful dialogue with the Commissioner for the Commission on Public Integrity (CPI) in areas of mutual interest, including investigations and training. The Iraqi IG system, the CPI, and the Board of Supreme Audit (BSA) lead Iraq's anti-corruption efforts to prevent fraud, waste, and abuse.¹⁹

Iraqi Inspector General System

The Iraqi IG system is modeled on the current U.S. system of federal inspectors general. With offices in each Iraqi ministry, the Iraqi IGs are appointed by the Iraqi Prime Minister, but work for their respective ministers.

During this reporting period, the Iraqi IGs focused on contracting for near-term training for their auditors, inspectors, and investigators. With the assistance of a SIGIR training curriculum review, the Iraqi IGs contracted for training at the American University in Beirut, Lebanon, in July. The SIGIR will assist in evaluating the success of the interim training.

In mid-July, the Inspector General from the Iraqi Ministry of Defense visited the United States and shared perspectives with the DoD IG, the SIGIR, and other inspectors general at the monthly meeting of the President's Council on Integrity and Efficiency (PCIE). Representing the IGs from all of the Iraqi Ministries, the Iraqi IG, who was appointed by the CPA Administrator following the enactment of CPA Order No. 57, presented the perspective of her fellow IGs on the current state of the Iraqi IG System. The Iraqi IG urged the development of relationships between U.S. departmental IGs and their Iraqi counterparts. The Iraqi IG also noted that, despite the evolving nature of the three-pillar anti-corruption initiative in Iraq, there was no disagreement on the need to create "an effective and enduring system to fight corruption in Iraq." The National Assembly has also supported anti-corruption measures through the appointment of a committee to oversee administrative efforts.

In July, the Iraqi IGs met with Iraqi National Assembly (Committee on Integrity). Each Inspector General gave a summary of work accomplished over the last year and the obstacles that must still be overcome. The Committee vowed to support the IG system and provide protection for IGs under the rule of law. The Committee announced its intent to change Order No. 57 to grant solely to the National Assembly the power to appoint and dismiss inspectors general. The IGs agreed with the concept as needed to maintain their independence and objectivity.

Commission on Public Integrity

The CPI is an independent part of the Iraqi government accountable for anti-corruption (investigations, prevention, and education) within the government as well as public outreach and non-government organization support. The CPI has a broad mandate established in CPA Order No. 55.

The CPI reports these highlights of its activity during the reporting period:

- bringing a series of high-level arrests in the Iraqi government—more than 30 senior (Director General or above) officials have been arrested on a variety of corruption charges, including this historic case:
 - In May 2005 the CPI brought the former Minister of Labor (Interim Iraqi Government) before a judge on charges of corruption. This is the first time since at least 1958 that a senior government official has been brought before an Iraqi court, in accordance with the rule of law and in a transparent manner. This case is currently pending.

- working 800 active cases with 77 CPI investigators—these cases show no apparent ethnic, religious, or tribal bias and are based on evidence gained and investigations conducted in accordance with Iraqi law
- developing legislative changes for the National Assembly, including inputs to the Iraqi constitution
- acquiring buildings and beginning the renovation process for the CPI Training Institute
- establishing a code of conduct, required to be signed by over 3 million Iraqi government employees
- initiating the implementation of financial disclosure requirements for all senior government employees
- publishing educational materials for use in primary and secondary schools and planning ethics and civics curriculum in cooperation with the Ministries of Education and Higher Education
- promoting the CPI Hotline and producing public service announcements

During the past year, the CPI has also provided training to the Iraqi IGs and the BSA, including curriculum developed by the DoD Defense Institute of Legal Studies and leading commercial audit organizations.

Challenges Facing the CPI

The CPI reports key concerns that may affect its operations:

- The number of corruption cases far outstrips the current CPI capacity and resources.
- Senior level officials in the Iraqi government under investigation or brought up on charges may be behind media, political, and physical attacks against the CPI.
- The National Assembly's legislative efforts and constitution writing may strengthen or weaken the CPI.

The CPI Commissioner serves as a counselor to the Ministry IGs for issues involving criminal allegations and subsequent investigations as well as a strong advocate of an effective IG system in Iraq.

Board of Supreme Audit

The Board of Supreme Audit (BSA) is an audit oversight institution with objectives similar to those of the U.S. Government Accountability Office. The BSA is gaining momentum in its core role of auditing government ministries, companies, and the state-owned banks in Iraq. The BSA is cooperating with the IRMO office for Financial and Fiscal Affairs to scrutinize the banks' accounts and management practices to focus oversight on restructuring efforts.

The BSA can do more to promote international accounting standards in the private sector as well as for government. The adoption of international accounting standards will be critical if Iraqi banks and companies are to gain the confidence of the international financial and business communities. The BSA also investigates complex financial transactions for money laundering and other potential corruption. The BSA plans to hire a new Director General who will be charged with establishing a Financial Intelligence Unit.

The BSA is working to address issues key to the development of its operations:

- the need to modernize its operational platform to provide an internal computer network and software applications that allow information to be shared and managed throughout the organization
- the need to hire additional experienced auditors to tackle a growing caseload of anti-corruption audits, such as the ones conducted recently on the contracting irregularities of the Iraqi Ministry of Defense

Security and Insurance

The management of area-wide security by U.S. military forces and Iraqi forces (undergoing IRRF-funded training) has not eliminated the need for site-specific security and for personal security of civilian contract employees. The threat to life and property from continuing insurgent attacks remains a major barrier to reconstruction and rehabilitation.

During this reporting period, the loss of contractor lives in Iraq remained consistent with levels reported during the past year, there were 18 new U.S. civilian deaths (mostly contractors) and 36 non-U.S. contractor deaths. The total number of claims grew by more than 30%, and death claims rose by 20%.

Although precise estimates are difficult to make, the threat to those involved in reconstruction and rehabilitation, along with the destruction to Iraqi infrastructure by sabotage, have impacted the effectiveness of the \$18.4 billion investment of the IRRF. Moreover, the already significant security costs will continue as long as the threat persists.

The Human Toll

Currently, two U.S. agencies in Iraq collect information about civilian contractor casualties in Iraq under separate statutory requirements:

- *The Division of Longshore and Harbor Workers' Compensation of the Department of Labor (DoL)* processes workers' compensation claims. These claims range from office injuries to claims for missing and deceased employees of contractors and subcontractors employed in U.S.-funded public works or service projects outside the United States (48 U.S.C. 1651). Claims are processed based on employment status, without regard to citizenship.

- *The Department of State (DoS)* is required to report the country and locality of all U.S. citizen deaths that occur because of unnatural causes [Sec. 204(c) of P.L. 107-228]. These reports do not include deaths of U.S. military personnel and U.S. government officials.

For contractors working overseas, the Defense Base Act (DBA) requires insurance coverage for employees performing work on U.S. government contracts. It functions as a workers' compensation program, providing disability and medical benefits for contractor injuries. For contractor deaths, DBA insurance provides for lost wages and/or survivor benefits. If it is determined that an injury or death was caused by a war-risk hazard and the insurance provider has not charged a war-risk premium, the U.S. government reimburses insurance carriers for their costs and assumes responsibility for future payments. The DoL administers DBA, ensuring that workers' compensation benefits are provided. The DoL tracks DBA death claims, which include both U.S. citizens and non-U.S. citizens who work for U.S. contractors.

During this reporting period, the SIGIR notes that the number of DBA claims continued to increase. The 36 new non-U.S. contractor DBA death claims received by the DoL and the 18 U.S. civilian deaths in Iraq (mostly contractor) reported by the DoS represent a rise from previous quarters. The SIGIR also notes these events that occurred in Iraq during this reporting period:

- Six Blackwater Security personnel died in an April 2005 helicopter crash.
- The U.S. military reported 201 deaths.
- DBA death claims for all U.S. and non-U.S. civilians working in Iraq rose to 330 as of June 30, 2005—20% higher than the 276 claims reported in the SIGIR April 2005 Report.
- Total DBA claims reported by the DoL, including both deaths and injuries, rose to 3,389 as of June 30, 2005—31% higher than the 2,582 reported by the SIGIR in April.

The rising number of DBA claims underscores both the dangers currently faced in reconstruction activities and the continuing costs arising from the current environment. DBA death claims tracked include both U.S. citizens and non-U.S. citizens who work for U.S. contractors. Analysis suggests that, since September 2004, there are more deaths of non-U.S. contractors than U.S. contractors. As shown in Figure 3-4, the reported deaths of non-U.S. civilians make up a larger portion of DBA death claims over time.

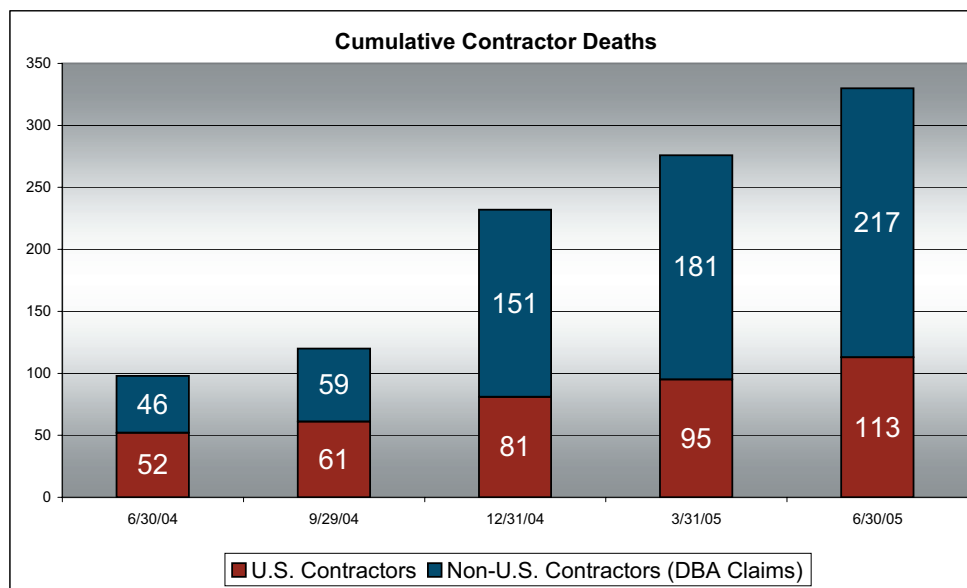


Figure 3-4

Since the end of the war on April 4, 2003, to June 30, 2005, the DoS has recorded 113 U.S. non-official civilian deaths in Iraq. Figure 3-5 identifies the sources of these deaths.

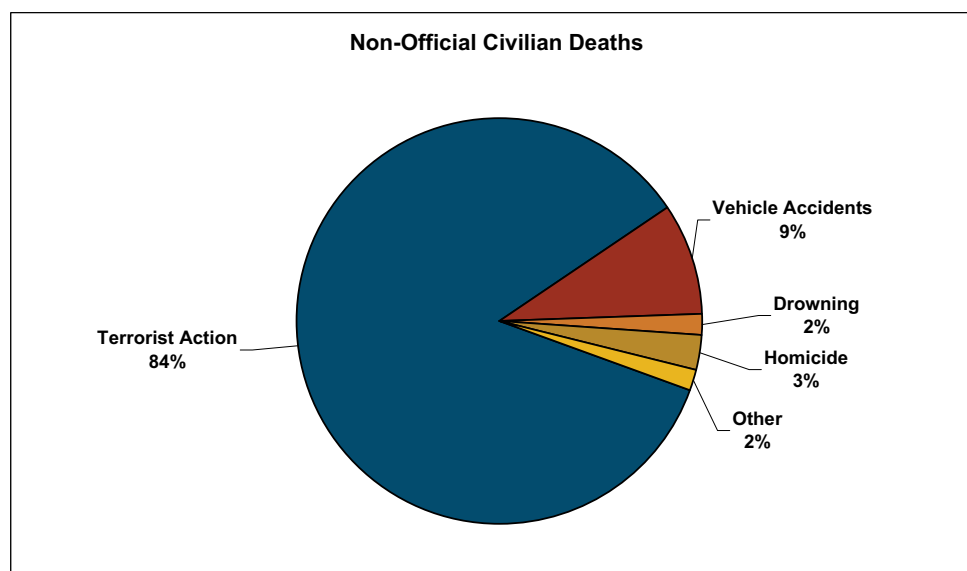


Figure 3-5

Insurance

On April 29, 2005, a GAO report, *Defense Base Act Insurance: Review Needed of Cost and Implementation Issues (GAO-05-280R)*, reported the need for a coordinated effort among affected agencies to identify actions that can address these challenges:

- It is difficult to determine whether all DBA insurance is purchased in a cost-effective manner.
- Implementation challenges hinder the ability of agencies to effectively provide workers' compensation coverage under DBA.
- The lack of reliable information on the number of contractors and cost of DBA insurance restricts the ability of agencies to make informed decisions on purchasing strategies for DBA.
- Despite the actions taken by agencies, these problems remain unresolved: confusion about when DBA applies, difficulty in enforcing DBA, and difficulty in processing claims.
- New challenges, such as growing numbers of contractors, have emerged since the DBA was enacted in 1941.

As a result, the GAO recommended that the Congress require the Office of Management and Budget (OMB) to coordinate with the DoD, DoS, DoL, and USAID to identify actions, including any necessary legislative changes, to address these issues:

- cost-effective options for acquiring DBA insurance
- methods for coordinating data collection efforts among agencies and contractors on the cost of insurance and other relevant information needed to make informed decisions
- consistent, collective, and collaborative application of the DBA across agencies by:
 - developing and disseminating guidance on when and to whom DBA applies
 - improving communications about the implementation of DBA and associated difficulties through informal networks, interagency working groups, conferences, forums, and Websites
 - identifying actions to address difficulties of administering the DBA
 - identifying potential means to address enforcement challenges
 - collecting data from contractor employees to facilitate claims processing
 - collecting and reporting information to the DoL on contractors performing overseas, including DBA coverage status

While the OMB agreed with the GAO's assessment and the DoD did not take exception to the factual information contained in the report, both agencies disagreed with the recommendations. The OMB stated that they were overly broad, and the DoD stated that they were too costly. In response, the GAO asserted that the recommendations were not overly broad; rather, they provide flexibility to agencies to deal with the full range of issues identified and allow them to address the growing use of contractors in overseas situations now and in the future proactively. The GAO continues to believe that a more coordinated

and comprehensive approach, involving all of the affected agencies, is necessary to address DBA cost and implementation issues.

Further Inquiry

On January 31, 2005, the U.S. Army Corps of Engineers (USACE) formalized a solicitation for a contract pilot program to manage the DBA centrally. These are the goals of the USACE pilot program:

- to address concerns about providing the best overall value to the nation in meeting the legal requirements of the DBA
- to encourage effective competition and assured availability and affordability of DBA insurance

In promoting a centrally managed program, the USACE has identified several impediments to providing DBA insurance economically and efficiently. For this solicitation, the USACE targeted early July 2005 as the end-date for the request for proposal period.

In addition, the USAID OIG provides the only available data on the current cost of security for U.S. contractors operating in Iraq. In the process of performing audits on costs incurred for completed contracts, the USAID OIG has tasked the Defense Contract Audit Agency to segregate disbursements for security costs from total audited costs. This tracking review will not account for differences in work location within Iraq, size of contract, or type of work, but will review the cost of security as a percentage of total costs in selected USAID contracts.

Finally, the Congress asked the GAO to examine the U.S. government's reliance on private firms to provide security in Iraq. The GAO's engagement focuses on:

- planning for the use of private security contractors in Iraq
- management controls established to provide visibility on security providers and security-related expenses
- the relationship between the DoD and private security contractors in Iraq
- the impact of private security providers on military retention

The GAO will issue a final report to the Congress by early August 2005. The SIGIR continues to discuss these issues with the GAO, but does not directly support the work.

Lessons Learned

The SIGIR Lessons Learned initiative continues to provide independent and objective leadership by coordinating recommendations that will promote improved economy, efficiency, and effectiveness in IRRF-administered programs.

The Lessons Learned team has completed the data collection phase of this effort, compiling more than 650 documents from these principal sources:

- *Interagency Audits and Oversight Observations*: audits, reports, reviews, and congressional testimonies conducted by U.S. Inspector General staffs
- *Industry Panels*: the perspectives of U.S.-based, professional services providers directly engaged in relief and reconstruction operations in Iraq (The Professional Services Council is coordinating participation in seminars and panels.)
- *Interviews and Questionnaires*: interviews and Individual Data Collection questionnaires conducted by the CPA historian and SIGIR staff assigned to U.S. government reconstruction organizations
- *Studies and Lessons Learned Summaries*: formal after-action summaries, studies, and lessons-learned reports conducted or sponsored by U.S. government agencies supporting Iraq relief and reconstruction operations

The Lessons Learned team has compiled more than 3,600 observations that capture the challenges, concerns, and risk factors facing U.S. government organizations engaged in relief and reconstruction operations in Iraq. The SIGIR continues to work within the interagency community to gather these findings and to coordinate integrated recommendations for improved policies, procedures, and implementation strategies.

Categorizing the Observations

A number of common themes have emerged from the cataloged observations. The Lessons Learned team categorized them into *domains* consistent with the Federal Enterprise Architecture and Business Management Modernization Program methodologies. The team identified these most commonly referenced areas:

- acquisition/contracting
- financial management
- human resources
- logistics
- planning and program management
- security
- strategic and organizational communications

Figure 3-6 shows the distribution of observations by domain.

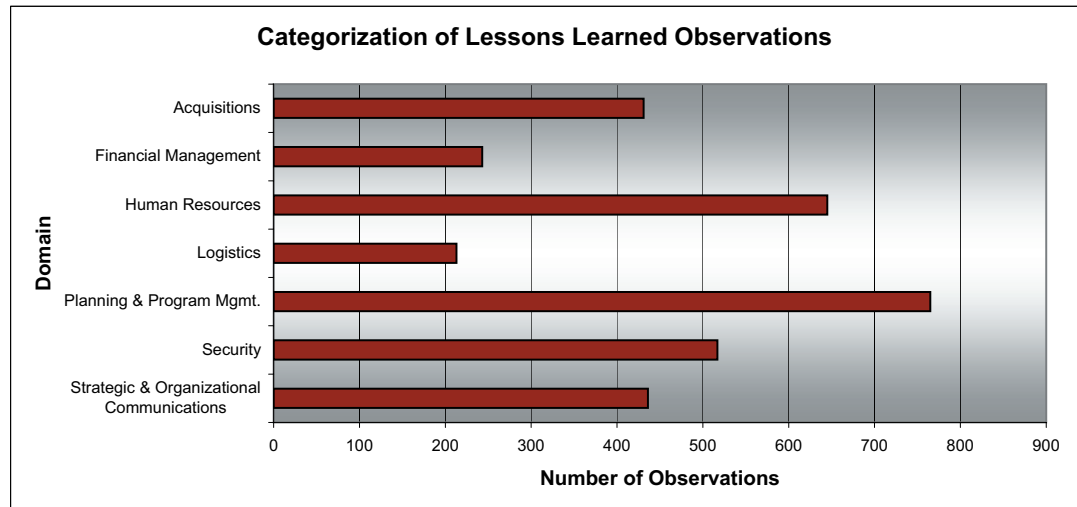


Figure 3-6

Next Steps: SIGIR Lessons Learned Forums

The SIGIR will host a series of Lessons Learned Forums in Washington, D.C., to focus on processes critical to the success of Iraq reconstruction operations and most closely aligned with the organization's charter to oversee the administration of IRRF-funded programs. Expert panels of executives from the U.S. government, industry, and academia will evaluate the findings compiled by the SIGIR and provide senior management recommendations to meet the challenges posed by the reconstruction of Iraq.

The SIGIR forums will focus on three domains:

- Human Resources (September 2005)
- Program and Financial Management (Fall 2005)
- Contracting and Acquisitions (Winter 2006)

Each seminar will result in a stand-alone report summarizing key leadership recommendations and highlighting the key challenges identified in panel discussions.

SIGIR Website

The SIGIR Website, www.sigir.mil, is an important component in providing transparency of operations. During this reporting period, the SIGIR focused on expanding the content provided in Arabic, enabling Arabic readers to have easier access to SIGIR products. As required by law, the SIGIR makes its Quarterly Reports available in both English and Arabic, and now SIGIR audit reports are also available on the site in Arabic. A new section of the site is completely navigable in Arabic.

The SIGIR currently posts these reports on the Website:

- all 6 Quarterly Reports to the Congress in English and Arabic
- all 23 SIGIR audits (8 in Arabic)

Figure 3-7 shows an updated view of the SIGIR Website.



Figure 3-7



SIGIR TEAM TOURS WATER PLANT—An assessment team from the SIGIR inspects a water treatment plant in central Iraq to examine construction progress associated with an upgrade of the facility, paid for with Iraq Relief and Reconstruction Funds.

Section 4

Public Law 108-106, as amended, requires the Special Inspector General for Iraq Reconstruction (SIGIR) to report to the Congress on the Iraq reconstruction efforts conducted by other government agencies. This section highlights the oversight activities of several agencies, including members of the Iraq Inspectors General Council (IIGC):

- Department of Defense
- Department of State
- U.S. Agency for International Development
- Government Accountability Office
- Defense Contract Audit Agency
- U.S. Army Audit Agency
- Federal Bureau of Investigation
- Defense Criminal Investigative Service

Other Agency Audits

The SIGIR formed the Iraq Inspectors General Council (IIGC) to aid in coordinating the oversight of Iraq relief and reconstruction programs. This section provides updates of the audits performed by IIGC member agencies.

Department of Defense

From April to June 2005, the Department of Defense Office of Inspector General (DoD OIG) performed limited audit activities somewhat related to Iraq relief and reconstruction. However, the DoD did not have any auditors in Iraq. The only DoD audit personnel who performed audit work in Iraq this quarter were detailed to the SIGIR.

Completed Audits and Assessments

Operations and Maintenance Funds for the FY 2004 Emergency Supplemental Appropriation Allocated to the Defense Information Systems Agency
(Report No. D 2005-053)

Completed on April 29, 2005, this audit evaluated accounting controls and procedures and validated and provided oversight of contingency operation costs incurred by DoD agencies supporting the Global War on Terrorism. The findings and recommendations of the report are For Official Use Only. Management concurred with the findings and recommendations.

Operations and Maintenance Funds for the FY 2004 Emergency Supplemental Appropriation Allocated to the Defense Logistics Agency
(Report No. D 2005-045)

Completed on May 9, 2005, this audit evaluated accounting controls and procedures and validated and provided oversight of contingency operation costs incurred by DoD agencies supporting the Global War on Terrorism. The findings and recommendations for the report are For Official Use Only. Management concurred with the findings and recommendations.

Ongoing Audits and Assessments

Contracts Awarded to Assist the Global War on Terrorism by the U.S. Army Corps of Engineers
(Project No. D2004CF-0186)

The objective of this audit is to examine contract requirements, determinations, and validation and award procedures for selected contracts and contract actions

awarded by the U.S. Army Corps of Engineers in support of the Global War on Terrorism. It is now in its draft report phase.

Audit of Contract Surveillance for Service Contracts
(Project No. D2004CF-0140)

The objective of this audit is to determine whether the government provides sufficient contract oversight for service contracts to ensure the contractors perform in accordance with the contract.

Ongoing Significant Reviews

Review of the U.S. Government's Relationship with the Iraqi National Congress
(Project No. D2005-DINTEL-012)

This review was announced on February 14, 2005. The objective is to respond to direction from the House Appropriations Committee. The specific objectives are classified. Research continues on the project.

Review of Detainee/Prisoner Abuse Investigations and Inquiries
(Project No. D2004-DINT01-0174)

This is a review of all closed DoD criminal and non-criminal investigations into detainee deaths and allegations of detainee abuse. The objective is to evaluate the investigative sufficiency, gaps in reporting detainee deaths, and allegations of detainee abuse.

DoS/DoD Joint Evaluation of Iraqi Police Training
(Project No. D-2005-DIP01E1-0034)

On October 7, 2004, the Department of State Office of Inspector General (DoS OIG) and the DoD OIG announced this joint assessment to review the shared responsibility of the two Departments to train and equip the Iraqi national police forces. The assessment is reviewing standardization issues, results and effectiveness measurements, leadership development, and retention rates. Fieldwork was completed in Jordan and Iraq in February and March 2005, respectively. The two Inspectors General expect to release the final report in July 2005.

Evaluation of Support to Mobilized Army National Guard and Army Reserve Units
(Project No. D-2004-DIP0E1-0127)

This review is evaluating whether the Army National Guard and U.S. Army Reserve units that deployed to Afghanistan and Iraq received adequate potable water, clothing, food, medical care, and access to communications with family members. The final report was expected to be released in July 2005.

Department of State

The DoS completed one audit involving Iraq relief and reconstruction since the SIGIR's April 2005 Report.

Completed Audits

Agreed-Upon Procedures Review of Indirect Rates and Equipment Delivery Charge Proposed by [a Department Contractor] and Review of Accounting System

(AUD/IQO-05-24), issued March 28, 2005

At the request of the Department, the DoS OIG performed this review. The DoS OIG did not take exception to the proposed indirect rates or equipment delivery charge, but had reservations as to whether the equipment delivery charge was properly treated as an indirect expense. The DoS OIG had similar reservations about treating the project management office as an indirect expense because the proposed staffing might not be consistent with the level of effort needed, which was not known at the time of the review.

The DoS OIG also found that the contractor did not have a contract cost accounting system in place. The DoS OIG recommended that if the proposal was successful, the contractor should be required to provide detailed procedures to ensure appropriate control over direct labor and other direct costs.

U.S. Agency for International Development

Since the SIGIR April 2005 Report, the U.S. Agency for International Development Office of Inspector General (USAID OIG) completed two audits involving Iraq relief and reconstruction, and began two new audits.

Completed Audits

The USAID OIG has completed one audit on activities in Iraq's electrical power sector and one audit on water and sanitation rehabilitation during this reporting period.

In addition to the USAID OIG audits discussed below, the Defense Contract Audit Agency (DCAA) completed nine financial audits for the USAID OIG on costs incurred and on labor, materials, and subgrant management under various contracts that the USAID OIG issued to the USAID/Iraq with a transmittal letter. These audits covered \$503,557,332 in USAID funds and questioned costs totaling \$14,227,276 for which the USAID/Iraq needs to determine allowability and take appropriate action. As of June 30, 2005, nine other DCAA audits were in process, which were also being performed at the request of the USAID OIG.

Audit of USAID/Iraq's Electrical Power Sector Activities

(Audit Report No. E-267-05-003-P), issued June 29, 2005

Audit objectives:

- Are the USAID/Iraq's electrical power sector projects achieving their intended outputs?
- Is the USAID/Iraq addressing institutional capacity-building in its projects to rebuild and rehabilitate Iraq's electrical power sector infrastructure?

The audit found that:

- The USAID's electrical power sector projects were not always achieving their intended outputs.
- Of the 22 projects reviewed, 7 (31.8%) had not achieved, or were not achieving, their intended outputs for reasons beyond USAID control.
- Two of the seven projects were impacted by the U.S. government's earlier efforts to reprogram government-wide infrastructure funding from the electrical sector to security and other priority areas, resulting in the cancellation of the two projects.
- Several other projects were experiencing implementation delays or were hampered by a lack of cooperation from Iraqi Ministry of Electricity staff, deteriorating security, and other factors.
- The USAID was found to be addressing institutional capacity-building under its electrical power sector projects, mostly through the provision of training; more needed to be done to address the problems and challenges both at the power plants and at the ministry level.

The OIG recommended that the USAID develop a multi-year strategy to strengthen the Ministry of Electricity's institutional capacity to operate and maintain this infrastructure.

Audit of USAID/Iraq's Water and Sanitation Rehabilitation Activities

(Audit Report No. E-267-05-004-P), issued June 30, 2005

Audit objectives:

- Are the USAID/Iraq's water and sanitation rehabilitation projects achieving their intended outputs?
- Is the USAID/Iraq addressing institutional capacity-building in its projects to rebuild and rehabilitate Iraq's water and sanitation sector infrastructure?

The audit found that:

- The water and sanitation rehabilitation projects were achieving intended outputs with some exceptions.

- Of the 34 projects reviewed, 30 projects (88%) achieved or were achieving their intended outputs. Four projects (12%) were not achieving their intended outputs because of a number of issues beyond the control of the USAID and its implementing partners: security conditions, problems accessing project sites, and lack of local government cooperation.

The audit also found that, for the items tested, the USAID addressed the issue of capacity-building in its projects to rebuild and rehabilitate Iraq's water and sanitation infrastructure through the provision of training and operation manuals. The USAID had taken steps to institute operations and maintenance support and training at the plant level.

Current Audits

The USAID OIG began two audits since the SIGIR April 2005 Report. These audits address Iraq's Cash Control Procedures and the Accuracy of Biographical Datasheets in Iraq.

Audit of USAID/Iraq's Cash Control Procedures

Audit objective: Did the USAID/Iraq manage its cashing operations in accordance with established regulations, policies, and procedures?

Audit of the Accuracy of Biographical Datasheets Provided by International Resources Group to USAID for Contracts in Iraq

Audit objective: Is selected information on the biographical datasheets provided to the USAID by International Resources Group accurate?

Government Accountability Office

Since the SIGIR April 2005 Report, the Government Accountability Office (GAO) has issued two reports and has ten ongoing audits on Iraq reconstruction.

Completed Reports

Defense Base Act Insurance: Review Needed of Cost and Implementation Issues

(GAO-05-280R), issued April 29, 2005

At the request of more than 100 members of the Congress, the GAO reviewed the issues related to the cost and availability of Defense Base Act (DBA) insurance for contractors. The GAO found in this review of these DBA issues that:

- It is difficult to determine whether all DBA insurance is purchased in a cost-effective manner.

- It is difficult to determine whether agencies' implementation challenges hinder their effectiveness in providing workers' compensation coverage under the DBA.
- The lack of reliable information on the numbers of contractors and cost of DBA insurance restricts the ability of agencies to make informed decisions on purchasing strategies for the DBA.
- Despite the agencies' actions, there are a number of unresolved problems, including confusion about when the DBA applies and difficulty in enforcing DBA and processing claims.

As a result, the GAO recommended that the Congress require the Office of Management and Budget (OMB), DoD, DoS, Department of Labor, and USAID to identify actions, including any necessary legislative changes, to address the following issues:

- identifying cost-effective options for acquiring DBA insurance
- developing methods for coordinating data collection efforts among agencies and contractors on the cost of insurance and other relevant information needed to make informed decisions
- facilitating consistent, collective, and collaborative application of the DBA across agencies by:
 - o developing and disseminating guidance on when and to whom the DBA applies
 - o improving communication about the implementation of the DBA and associated difficulties through informal networks, interagency working groups, conferences, forums, or websites
- identifying actions to address difficulties with administering the DBA, such as:
 - o identifying potential means to address enforcement challenges
 - o collecting data from contractor employees to facilitate claims processing
 - o collecting and reporting information to the DoL on contractors performing overseas, including DBA coverage status

While the OMB agreed with the GAO's assessment and the DoD did not take exception to the factual information contained in the report, both agencies disagreed with the recommendation. The OMB stated it was overly broad and the DoD stated it was too costly. In response, the GAO stated it does not believe that the recommendation was over broad, rather it provides flexibility to agencies to deal with the full range of issues identified, and it allows them to proactively address the government's growing use of contractors in overseas

situations now and in the future. The GAO continues to believe that a more coordinated and comprehensive approach, involving all of the affected agencies, is necessary to address DBA cost and implementation issues.

Defense Management: Processes to Estimate and Track Equipment Reconstitution Costs Can Be Improved

(GAO-05-293), issued May 5, 2005

The DoD uses a two-phased process to develop supplemental budget estimates to reconstitute equipment. The GAO reviewed this process for the FY 2004 supplemental budget to determine:

- the extent to which the process produced reliable estimates of reconstitution requirements in the FY 2004 supplemental budget
- whether the DoD is accurately tracking and reporting reconstitution costs

The GAO found that the DoD's two-phased process to develop its FY 2004 cost estimates for equipment reconstitution contained weaknesses that produced errors. These errors may result in misstatements of future-year reconstitution cost requirements. The model DoD used to estimate costs in the first phase of the process generated unreliable estimates for two main reasons:

- First, the model can overstate aircraft and ship reconstitution costs because these costs are covered in two different sections of the model. As a result, the model's estimate for Air Force aircraft reconstitution was overstated by more than \$1 billion.
- Second, there is uncertainty over what maintenance requirements the model covered. The Office of the Secretary of Defense (OSD) and the Services developed their requirements with the understanding that the model did not calculate all maintenance requirements. The GAO learned that the model may duplicate some requirements that the Services manually calculated and included in their cost estimates. Consequently, the DoD cannot have confidence that its equipment reconstitution budget estimate is reliable.

The DoD has not accurately tracked and reported its equipment reconstitution cost because the Services are unable to segregate equipment reconstitution from other maintenance requirements as required. As a result, the DoD cannot accurately report the cost of equipment reconstitution and, consequently, the total cost of the Global War on Terrorism.

Recommendations for Executive Action:

To correct the weaknesses that the GAO identified in the process used to estimate equipment reconstitution costs when developing its FY 2004 supplemental budget request, the GAO recommended that the Secretary of Defense take these five actions:

- Direct the DoD Comptroller to revise its cost model to ensure that costs covered by the model's operating tempo cost elements are not duplicated by costs in the model's reconstitution cost elements.
- Direct the DoD Comptroller to clearly establish what equipment maintenance requirements should be covered by the cost model and communicate this information to ensure that the model's calculations reflect only these maintenance costs.
- Direct the Secretary of the Army to establish a step in its supplemental estimating process to offset the estimate with the baseline budget to improve future contingency funding estimates.
- Direct the DoD Comptroller to clarify its supplemental budget guidance to the Services on what types of maintenance requirements should and should not be included as equipment reconstitution when developing the supplemental budget.
- Direct the DoD Comptroller to ensure that all potential equipment reconstitution requirements are considered when developing supplemental budget requests by allowing the Services to include anticipated equipment losses—both operational losses and maintenance washouts—in their supplemental budgeting process.

To ensure that the Congress has a clear insight into the cost of equipment reconstitution, the GAO also recommends that the Secretary of Defense direct the Services, in conjunction with the Defense Finance and Accounting Service (DFAS), to develop comprehensive and consistent methods for tracking and reporting equipment reconstitution obligations, including:

- developing a mechanism within the Air Force for identifying, accumulating, and reporting its equipment reconstitution obligations
- refining the processes used by the Navy and Army to identify obligations that are incurred for equipment reconstitution

Current Audits

United Nations Oil for Food: Oversight and Accountability

UN Security Council Resolution 986 established the Oil-for-Food program in 1996 to allow Iraq to use oil revenues to purchase certain goods after sanctions were imposed in 1990 following Iraq's invasion of Kuwait. The overall objectives of the humanitarian assistance program were to prevent Iraq from having weapons of mass destruction while allowing Iraq to use its oil revenues to import food, medicine, and other needed supplies.

The GAO, other congressional investigators, the Defense Intelligence Agency Iraq Survey Group, and others have reported that Iraq gained billions in illicit revenues through smuggling and corruption. Allegations have also surfaced about misconduct by UN and contractor personnel involved in the program. In

October 2004, the Congress mandated that the GAO review the program (P.L. 108-375).

- What programs and activities did resolution 986 authorize?
- What were the internal controls and external challenges associated with the selling of Iraq's oil?
- What were the internal controls and external challenges associated with the humanitarian assistance program?
- What is the mandate of the UN Compensation Commission, and how is it structured to carry it out?

Private Security Contractors

This work is in response to congressional interests related to the reliance of the U.S. government and its contractors on private firms to provide security in Iraq:

- To what extent have U.S. government agencies and contractors working in Iraq acquired security services from private providers?
- To what extent have U.S. military and private security providers in Iraq developed a cooperative working relationship?
- To what extent have U.S. government agencies assessed the costs associated with using private security providers on reconstruction contracts?

The report also assessed the impact of the increased use of private security providers on attrition in key military skills.

DoD Logistics Transformation Initiatives

The DoD has undertaken logistics improvement initiatives, but has not achieved a logistics system responsive to the asymmetric threat the DoD now faces. Earlier logistics transformation efforts lacked an overarching plan to tie numerous service initiatives to the DoD's strategic logistics objectives:

- To what extent has the DoD defined the desired end-state for its initiatives and identified goals, resources, and timeframes?
- How successful have logistics initiatives been to date, and what are the challenges/barriers to broader implementation?
- To what extent are the DoD's initiatives integrated, and do they complement the DoD's overall force transformation plans?
- To what extent have these initiatives improved the effectiveness of support to the warfighter?

Use of Funds in Support of the Global War on Terrorism

Since September 11, 2001, the Congress has appropriated about \$275 billion for the Global War on Terrorism. Spending is running about \$6 billion per month, based on April 2005 data. The GAO's objectives are to determine:

- whether DoD's reported war costs are based on reliable data
- the extent to which DoD's financial management guidance applies to war spending
- whether spending controls for the war can be strengthened as operations mature

Improving Iraq's Security

As of March 2005, the United States had obligated about \$5.8 billion to train, equip, and develop Iraqi security forces and transfer security responsibilities to them. The President requested an additional \$6 billion in early 2005 to accelerate this process.

- What is the current multinational force strategy for transferring security missions to Iraqi security forces?
- What are the challenges to this transition?
- What are the current trends in the security situation in Iraq?

Use of Airlift Capacity for Operations in Afghanistan and Iraq

The DoD's ability to airlift cargo is critical to supporting contingency operations, such as Operation Enduring Freedom (OEF) and Operation Iraqi Freedom (OIF).

- How did the Air Mobility Command manage the use of airlift capacity, including the Civil Reserve Air Fleet, for OIF and OEF and for current containment operations?
- What barriers exist, if any, to maximizing airlift capacity?

Iraq's Elections

U.S. policy is that credible Iraqi elections resulting in a representative government are critical to Iraq's future. On January 30, 2005, more than 8 million Iraqis voted in the first of three national elections that will establish a permanent government. By the end of 2005, the United States will have obligated more than \$150 million in civilian efforts to support the three elections during Iraq's political transition. The report provides information on the following:

- How did the Iraqi government prepare for, and what has been the outcome, of the January Iraqi elections?
- What has been the nature and extent of U.S. assistance for Iraqi elections?
- What were the improvements that organizations participating in the elections process identified?

Iraq Water and Sanitation

Since the fall of the Hussein regime, the United States has recognized

improved essential services as critical for achieving a stable Iraq. As of March 2005, the United States has allocated about \$2.4 billion for water and sanitation efforts.

- What are the U.S. government's goals for rehabilitating Iraq's water and sanitation sector, and how is progress measured?
- What is the status of the U.S. reconstruction effort in the water and sanitation sector?
- What provisions have U.S. government agencies made to assist the sustainability of completed projects?

Reconstruction Efforts in Iraq

The United States has committed more than \$24 billion to reconstruction in Iraq. This engagement will focus on U.S. progress in reconstruction of Iraq's power, oil, water, and health sectors. The GAO will also track U.S. funding.

- What are the amounts, sources and uses of funding that have been made available for Iraq relief and reconstruction?
- What are the status, progress, and challenges of the oil, power, water, and health sectors of the U.S. relief and reconstruction effort in Iraq?

Post-transition Management of Iraq Reconstruction

Since Iraq regained sovereignty in June 2004, the Secretary of State has assumed responsibility from the DoD and the Coalition Provisional Authority for setting requirements and priorities for managing the U.S. reconstruction program in Iraq, including \$18.4 billion in FY 2004 emergency funding.

- How is the U.S. government organized to supervise and direct the reconstruction effort in the post-transition phase?
- How are program management contracts used to manage and support the reconstruction effort in Iraq?
- What factors are challenging U.S. efforts to rebuild Iraq, and how are they being addressed?

Defense Contract Audit Agency

The DCAA plans and performs work on a fiscal year basis. The DCAA's services include professional advice to acquisition officials on accounting and financial matters to assist them in the negotiation, award, administration, and settlement of contracts.

In addition to the DCAA's involvement in the negotiation and award of contracts, significant resources are also dedicated to overseeing the allowability, allocability, and reasonableness of incurred and billed costs.

Procedures that govern the costs incurred in-country are also tested through reviews of contractor timekeeping, subcontract management, and cash management and disbursement. Finally, to ensure that adequate internal controls are in place regarding the contractor's policies and procedures, the DCAA performs audits associated with critical internal control systems, with an emphasis on estimating, subcontract management, and billing systems.

Table 4-1 shows both the Iraq-related audits closed during FY 2004 and the audits closed, opened, and planned in FY 2005 (as of June 30, 2005).

DCAA Audits Related to Iraq for FY 2004 and FY 2005, as of June 30, 2005				
	FY 2004	FY 2005	FY 2005	FY 2005
	Closed	Closed	Open	Planned
Price Proposals (1)	128	133	27	5
Agreed-Upon Procedures Price Proposal (2)	113	47	0	0
Other Special Requested Audits (3)	123	138	173	16
Incurred Cost (4)	1	3	21	14
Labor Timekeeping (5)	59	61	37	14
Internal Controls (6)	47	48	52	36
Preaward Accounting Survey (7)	30	16	3	0
Purchase Existence and Consumption (8)	15	10	20	8
Other (9)	51	61	88	14
Total	567	517	421	107
Notes: 1. Price Proposals – Audits of price proposals submitted by contractors in connection with the award, modification, or repricing of government contracts or subcontracts 2. Agreed-Upon Procedures Price Proposal – Evaluation of specific areas, including actual labor and overhead rates and/or cost realism analysis, requested by customers in connection with the award of government contracts or subcontracts 3. Other Special Requested Audits – Audit assistance provided in response to special requests from the contracting community based on identified risks 4. Incurred Cost – Audits of costs charged to government contracts to determine whether they are allowable, allocable, and reasonable 5. Labor Timekeeping – Audits to determine if the contractor consistently complies with established timekeeping system policies and procedures for recording labor costs 6. Internal Controls – Audits of contractor internal control systems relating to the accounting and billing of costs under government contracts 7. Preaward Accounting Survey – Preaward audits to determine whether a contractor's accounting system is acceptable for segregating and accumulating costs under government contracts 8. Purchase Existence and Consumption – The physical observation of purchased materials and services and related inquiries regarding their documentation and verification of contract charges 9. Other – Significant types of other audit activities, including financial capability audits and Cost Accounting Standards compliance audits				

Table 4-1

U.S. Army Audit Agency

The U.S. Army Audit Agency (USAAA) completed two audits during this reporting period and currently has three other audits ongoing.

Completed Audits

Program Management in Support of Iraq Reconstruction

(Project Code: A-2004-AMA-0606.000), issued May 26, 2005

The former Acting Secretary of the Army requested this audit. The overall objective was to determine if the Army and the Project and Contracting Office (PCO) established controls and sound business processes to mitigate previously identified high-risk areas, including:

- contracting plans for awarding task orders against existing contracts
- acquisition plans for obligating the remaining Iraq Relief and Reconstruction Fund (IRRF) and measuring obligation rates
- PCO efforts to mitigate risks and cost growth on undefinitized contracts
- PCO plans to oversee reconstruction contracts (for example, contractors overseeing contractors)

In summary, the audit found that the Army and the PCO have put many controls in place to mitigate previously identified high-risk areas. However, additional actions are needed to strengthen controls:

- Although the PCO established controls for monitoring and measuring obligations, additional controls were needed to account for all the DoD obligations and to measure the progress of the FY 2004 IRRF program.
- The PCO established controls to help definitize contracts in a timely manner, but those controls were not fully effective.
- The PCO controls for using program management support contractors were generally effective, but additional controls were needed to reduce the risk associated with contractors performing inherently governmental functions, real or perceived conflicts of interests with contractors overseeing contractors, and award fee plans.

The Army concurred with the recommendations, which should give the Army better assurance that it is properly controlling and executing the FY 2004 IRRF program.

Commanders' Emergency Response Program (CERP) and Quick Response Fund (QRF)

(Project Code: A-2005-ALE-0191.000), issued May 26, 2005

The Commander of the Multi-National Security Transition Command-Iraq (MNSTC-I) requested this audit. Objectives of the audit include:

- Were funds for the CERP and the QRF received, accounted for, and reported according to applicable laws and regulations?
- Were disbursements consistent with the intent of the charter or implementing guidance?

In summary, the audit team reached positive conclusions on both objectives. But the initial conclusion to the objective on whether funds were disbursed according to the intent of the charter and implementing regulations was negative because command personnel did not retain copies of key documents (receiving reports and payment vouchers). Command personnel working with the local finance office, however, were able to obtain properly signed copies of receiving reports and disbursement vouchers attesting that:

- The command received contracted goods and services according to contract specifications.
- Contractors signed for payment and certifying officials approved the payments.

USAAA personnel verified the accuracy of the local records by comparing local copies with those on file with the DFAS in Rome, New York. The Army concurred with the recommendations.

Current Audits

Audit of Fund Accountability for Iraq Relief and Reconstruction Fund 2 (IRRF2)

(Project Code: A-2005-ALA-0240.000)

The former Acting Secretary of the Army requested this audit. The audit will focus on fund control and accountability over the IRRF2 for reconstruction activities and Operation and Maintenance Army funds for PCO administrative expenses. The overall objective is to make sure the Army and PCO have effective controls and sound business processes in place to properly account for that portion of the \$18.4 billion in IRRF2 that the DoD activities execute. Specific objectives include:

- Do the PCO's financial management system and processes have the controls needed to make sure that commitments, obligations, and disbursements are accurately recorded? This includes ensuring that the PCO used and recorded the funds for the proper sector.
- Does the PCO have adequate controls in place to make sure that operating costs and program costs are properly allocated and recorded?
- Can the PCO's financial management system and processes accommodate Army and PCO plans to decentralize contract award and project management?

Field work has been completed, and the draft report is being prepared for issue in July 2005.

Follow-up of Commanders' Emergency Response Program (CERP) and Quick Response Fund (QRF)

(Project Code: A-2005-ALE-0376.000)

The Commander of the MNSTC-I requested this audit. Objectives of the audit include:

- Were FY 2005 funds for the CERP and the QRF received, accounted for, and reported according to applicable laws and regulations?
- Were disbursements consistent with the intent of the charter or implementing guidance?
- Did the MNSTC-I adequately implement agreed to recommendations of Audit A-2005-ALE-0191.000, and did corrective actions fix problems?
- Did the MNSTC-I have an effective follow-up system for tracking the implementation of corrective actions until fully implemented?

A draft report was expected to be issued in early July 2005.

Audit of Logistics Civil Augmentation Program

(Project Code: A-2005-ALS-0340.000)

The Commander, Multi-National Force-Iraq requested this audit. Preliminary audit planning began on January 3, 2005, and audit work began in Kuwait and Iraq on May 3, 2005. (In-country work was delayed at command's request.) The audit focuses on evaluating the adequacy of the Logistics Civilian Augmentation Program (LOGCAP) throughout the Iraq area of operations. The specific objectives include:

- Are the services acquired under the LOGCAP contract reasonable and cost-effective solutions for satisfying force requirements?
- Are adequate management structures in place to plan, acquire, and manage services obtained under the LOGCAP contract?
- Is the contract administration over LOGCAP work in Iraq adequate?
- Are adequate management/internal controls in place over LOGCAP operations in Iraq, especially those areas highly susceptible to fraud, waste, and abuse?
- Does adequate information exist to enable higher management to provide sufficient oversight over LOGCAP operations in Iraq?

During the initial work, the audit team traveled to several operating bases in Iraq, the principal sites of contractor operations in Kuwait, and the prime contractor's home office in Houston, Texas. The team also requested and received authority from the DoD OIG (Auditing) to audit:

- the Defense Contract Management Agency's LOGCAP contract administration operations in Iraq

- the Defense Logistics Agency's food service operations in support of the Iraq area of operations

The audit is currently focusing on the Army's contract cost-monitoring process, program management structure, base closure process, material transportation and distribution processes, and food operations. Draft reports will be issued imminently. The team identified other areas for more intense survey work and will likely start audit work in those areas after completing the current audit areas.

The USAAA currently has 14 auditors in Iraq and Kuwait working on the audit of the LOGCAP.

Other Agency Investigations

Federal Bureau of Investigation

The FBI reported four open and pending cases involving activities associated with Iraq. During the reporting period, the FBI did not close or refer any cases to other law enforcement agencies. The SIGIR is working one of these cases in conjunction with the FBI.

United States Agency for International Development

During this reporting period, the USAID did not open any new cases. The USAID has closed five cases. The USAID has six ongoing cases: five are on program integrity, and one is on employee integrity.

Closed Cases

The USAID closed five cases during this reporting period.

Examples of Closed Cases:

- *Program Integrity:* It was alleged that a USAID contractor firm had been inflating invoices submitted to the USAID for the purchase of certain commodities in Iraq. It was further alleged that the invoices were inflated to pay kickbacks to employees of the contractor. However, the investigation revealed no instances of misconduct that would warrant a criminal or civil prosecutorial referral. In addition, no evidence was found to substantiate other allegations of misconduct that surfaced during the course of the investigation regarding conflicts of interest. Accordingly, the case was closed.
- *Employee Integrity:* This case was an employee integrity matter involving an employee assigned to Iraq. The investigation did not substantiate the allegations and was closed.

Ongoing Cases

The USAID currently has six ongoing cases: five are on program integrity and one is on employee integrity.

Examples of Ongoing Cases:

- *Program Integrity*
 - A USAID contractor was alleged to have submitted false and/or fraudulent costs associated with work in Iraq. In addition, information

was developed indicating that this contractor may have used USAID funds to make improper payments to Iraqi government officials.

- A contractor was alleged to have knowingly used non-U.S. carriers to transport equipment from the United States to Iraq in violation of the terms and conditions of its contract.
- An allegation of ethical misconduct involving an employee assigned to Iraq was received. The active investigation was concluded, and the results were forwarded to the agency for consideration of appropriate administrative action.
- A contractor was alleged to have been inflating the cost it was charging the USAID. The matter has been referred to the OIG/Audit, which will be initiating an audit relative to the allegations. The case is now in tracking status pending audit results.
- A subcontractor on a USAID-funded prime contract was alleged to have been engaged in a variety of financial irregularities.
- *Employee Integrity*
 - Employees of a USAID contractor are alleged to have solicited kickbacks in exchange for awarding subcontracts for work in Iraq.

Defense Criminal Investigative Service

On October 31, 2004, the Defense Criminal Investigative Service (DCIS) ceased operations in Baghdad, Iraq.

Open Cases

The DCIS currently has five open cases and one open project.

Department of State

The DoS OIG reported three open and pending cases involving activities associated with Iraq. The DoS OIG is currently working two joint investigations with the SIGIR. The DoS has no criminal investigators assigned to Iraq and is providing investigative support from its office in Rosslyn, Virginia.